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CONSTRUCTION-DIFFERENTIAL SUBSIDY PAYBACK

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HEARING

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BEFORE THE

SUBCOMMITTEE ON MERCHANT MARINE

OF THE

COMMITTEE ON
MERCHANT MARINE AND FISHERIES
HOUSE OF REPRESENTATIVES

NINETY-NINTH CONGRESS

FIRST SESSION

ON

H.R. 2485

TO PROVIDE FOR THE EQUITABLE REPAYMENT OF CONSTRUCTION-DIFFERENTIAL SUBSIDY

H.R. 2550

TO AMEND SECTION 506 OF THE MERCHANT MARINE ACT, 1936, TO PERMIT PERMANENT PAYBACK OF CONSTRUCTION-DIFFERENTIAL SUBSIDY

MAY 23, 1985

Serial No. 99-16

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CONSTRUCTION-DIFFERENTIAL SUBSIDY PAYBACK

THURSDAY, MAY 23, 1985

House of Representatives,
Subcommittee on Merchant Marine,
Committee on Merchant Marine and Fisheries,
Washington, DC.

The subcommittee met, pursuant to notice, at 10:28 a.m., in room 1334, Longworth House Office Building, Hon. Mario Biaggi (chairman of the subcommittee) presiding.

Present: Representatives Biaggi, Anderson, Tallon, Mikulski, Jones, Snyder, Shumway, Fields, McKernan, Saxton, and Lent.

Staff present: Cyndy Wilkinson, Greg Lambert, Linda Livingston, Ed Welch, Gerry Seifert, Chris Goebel, Kip Robinson, Gwen Lockhart, and George Pence.

Ms. **Mikulski** [acting chairman]. Good morning.

Today the Merchant Marine Subcommittee meets to consider the issue of repayment of construction-differential subsidies.

The hearing will be chaired by its ranking Democratic member, Mr. Biaggi. However, Mr. Biaggi is testifying at another committee hearing and, in the interest of expediting both the committee's work and not delaying our witnesses, Mr. Biaggi has asked me to open this meeting.

With unanimous consent, I would like to reserve the right for Mr. Biaggi to make his own opening statement or include it in the record.

Hearing no objection, so ordered.

[Statement of Mr. Biaggi follows:]

Statement of Hon. Mario Biaggi, Chairman, Subcommittee on Merchant Marine

Good morning. Today the Merchant Marine Subcommittee meets to consider the issue of repayment of construction-differential subsidy.

The Construction-Differential Subsidy Program was established by the 1936 Merchant Marine Act. It subsidized the higher cost of construction in the U.S. to enable U.S. operators to obtain their vessels at approximately the same cost as their foreign competitors. The CDS Program also benefitted U.S. shipyards by generating commercial work.

The act prohibited vessels built with CDS from participating in the domestic trade except in limited circumstances for short periods of time. The act did not specifically address whether a subsidized carrier could totally repay his construction subsidy and be freed from the domestic trading restrictions. However, a series of administrative and judicial decisions has brought us to the point where the Maritime Administration is empowered to accept total repayment and a vessel can permanently enter the trade. Earlier this month the Department of Transportation promulgated rules permitting an owner of a CDS-built vessel to permanently enter the trade if within one year he repays the CDS proportionate to the remaining economic life of the vessel, together with an appropriate amount of interest.

The Department of Transportation and the owners of CDS-built vessels view this as a reasonable compromise, since it only permits repayment for a limited period of time, and required the payment of interest. Domestic operators argue that the rule would cause them severe economic harm.

In light of these concerns, I introduced a bill, which adopted some of the procedures in the rule such as a limited window for repayment. However, it also provides that vessels will only be permitted to enter the trade for half their remaining economic life.

Chairman Jones has introduced a bill, which is another attempt to reach a fair and equitable compromise protecting the interests of all parties. That legislation would augment the current six month waiver procedure and provide for full repayment over a protracted period.

Today, we will hear reaction to these three proposals. Also, I encourage the witnesses to examine other approaches to assist us in reaching a fair result.

OPENING STATEMENT OF HON. BARBARA A. MIKULSKI, A U.S. REPRESENTATIVE FROM MARYLAND

Ms. MIKULSKI. I am happy that we are considering the construction-differential subsidy issue today and that we will be receiving testimony from various sectors of our domestic marine industry on this subject.

I am happy that Mr. Biaggi is doing this, and I look forward to working with him and our full committee chairman, Mr. Jones, toward a solution on this problem.

I do not have a neutral view on this. As my colleagues know, the CDS payback issue has been one which this committee has had a strong interest in since the Department of Transportation first proposed a payback rule in early 1983. I have generally opposed efforts by DOT to permit U.S. shipping companies to repay their CDS in return for the right to enter the Jones Act trade. That position is based on a number of economic and national security consequences which a payback would have.

However, Congress was very clear in its intent in passing the Merchant Marine Act of 1970 that the law provided instruction and operating subsidies to shippers for vessels built in the United States to be used exclusively for foreign trade. In providing such subsidies, Congress recognized the economic dilemma of American operators who wanted to have U.S. ships in the foreign trade but faced competitive disadvantages if they had to build those ships in the American shipyards.

I have many questions which I hope to ask during the hearing, which I will not bring up in my opening statement.

I ask unanimous consent that my opening statement be included in its entirety in the record.

[Statement of Ms. Mikulski follows:]

STATEMENT OF HON. BARBARA A. MIKULSKI, A U.S. REPRESENTATIVE FROM MARYLAND

This morning the subcommittee will receive testimony from various sectors of our domestic maritime industry on CDS payback, an issue which has major consequences for the future of the U.S. Merchant Marine.

I commend our subcommittee chairman, Congressman Biaggi, for scheduling these hearings before the DOT rule on CDS payback takes effect next month.

I look forward to working with him, and our full committee chairman, Congressman Jones, towards a solution to the problems we are faced with on this issue.

As my colleagues know, the CDS payback issue has been one which this committee has had a strong interest in since the Department of Transportation first proposed a payback rule in early 1983.

I have generally opposed efforts by DOT to permit U.S. shipping companies to repay their construction subsidies in return for the right to enter the Jones Act trade.

That position is based on a number of economic and national security consequences which such a payback would have.

Congress was very clear in its intent in passing the Merchant Marine Act of 1970. That law provided construction and operating subsidies to American shippers for vessels built in the United States and to be used exclusively in the foreign trade.

In providing such subsidies, Congress recognized the economic dilemma of American operators who wanted to have U.S. ships in the foreign trade, but faced competitive disadvantages if they had to build those ships in American shipyards.

By providing both CDS and ODS, Congress reaffirmed its traditional support for the U.S. Merchant Marine and the role of this Nation as a leader in international shipping.

At the same time, the 1970 Act reduced the amount of capital, and therefore investment risk, which U.S. operators in the foreign trade would have to provide to begin new ship construction and operation.

In enacting the 1970 Act, however, Congress did not intend to damage the investment climate for domestic ship operators who wanted to construct U.S. vessels for the Jones Act trade.

As a result, the initial question which I believe our subcommittee should ask is whether the proposed DOT rule is in keeping with intent of the CDS program as envisioned by this committee and the entire Congress?

In addition, it is crucial that we examine the economic implications of this rule. Some have contended that the U.S. Treasury would receive a windfall of nearly $300 million from this enactment of this rule.

Any benefits from repayment however, need to be weighed against the number of defaults on Title XI loan guarantees from domestic ship owners which would be displaced by the rule.

When factoring in the amount of Title XI defaults, and the lost tax revenues due to increased unemployment caused by American seamen who would lose their jobs due to this rule, the Treasury's windfall is virtually non-existent.

Finally, the subcommittee must be honest about the national security problems which this rule creates.

Our sealift capacity will be severely damaged by this rule because a significant number of militarily-useful tankers will be permanently displaced. The ones we will allow into the Jones Act will be far too large, for the most part, for Naval support purposes.

Second, the overtonnaging in the Alaskan oil trade caused by this rule will further erode future domestic tanker ship construction. The effect on domestic shipyards, according to many, will be dramatic, further weakening our shipyard mobilization base.

In light of these problems, I look forward to our discussions today.

I hope they are candid, and that we can work toward a solution to the CDS repayment question which: first, protects the integrity of the Jones Act; second, the investment climate for domestic ship construction; third, the maximum amount of American seafaring jobs; and finally, our Nation's sealift capacity and readiness. Thank you.

Ms. MIKULSKI. The Chair now recognizes Mr. Snyder, our ranking minority member. Then when Mr. Jones gets settled, we will recognize him.

STATEMENT OF HON. GENE SNYDER, A U.S. REPRESENTATIVE FROM KENTUCKY

Mr. SNYDER. Thank you, Madam Chairman.

Welcome to the witnesses who will be testifying today, all of whom look quite familiar by now. A particular welcome to Assistant Secretary Matt Scocozza, who I am sure is glad to be here again, even though he is up to his elbows in TWA and Icahn, as we know from our discussions yesterday.

I suspect when you get back to the Nassif building, you are going to be quite effusive in your thanks for having had the opportunity to testify again on this issue.

Madam Chairman, I have to confess to a certain sense of mystery as to why any of us have the opportunity to again revisit the CDS repayment issue. I quite fully understand and appreciate Chairman Biaggi's reasons for having introduced H.R. 2485. However, frankly, I believe the spirit of compromise and cooperation he has sought to foster has been a one-way street. Witness the actions which occurred in the House Appropriations Committee just this Tuesday, on yet another attempt to block the implementation of the DOT rule. I don't consider that action on the part of the opponents as being particularly compromising or cooperative.

I, for one, Madam Chairman, while admiring the stamina of Chairman Biaggi's pursuit of legislative compromise on this issue, have quite frankly lost some patience with those who are opponents to CDS repayment and their delaying tactics. I don't see any willingness on the part of those who are opponents to cooperate with Chairman Biaggi or any other members who are attempting to work out some sort of a compromise. I just see it as a continuing effort to stop things from proceeding.

Let's look briefly at some of the benefits associated with the DOT rule: $277 million in deficit-reducing payments to the U.S. Treasury; additional savings in reduced operating-differential subsidies; $823 million in reduced cost of transporting Alaska North Slope oil over 10 years just because of increased efficiencies in the CDS ships; and a possible $2.5 billion in additional savings to shippers because of reduced rates.

DOT estimates that a portion of these benefits might be offset by $170 million in Federal outlays, primarily to pay off title XI loan guarantees—exposure on vessels which might be bumped from the trade, I assume.

On balance, however, the projected benefits present a most compelling argument for allowing—indeed, encouraging—the CDS repayment rule to go forward.

Madam Chairman, I would like to remind the subcommittee of one additional fact. The first concurrent resolution on the budget which the House is now considering—and I don't think I am presumptuous in assuming that the Budget Committee's resolution will be the one that will be adopted today—both it and the Latta substitute assume CDS payback, as does the Senate budget resolution, which has already been adopted.

After 20 years here, if I understand the conference procedure properly, if in fact both the House and the Senate are in agreement on that item, I am not even sure that it would be "conferenceable." I think that we are going to have a budget resolution, assuming that we pass any budget resolution today, and I am assuming that your budget resolution or the House Budget Committee's budget resolution is going to be adopted, it seems to me we are going to have CDS payback. Since it is not subject to reconciliation, however, in the House budget resolution, as it is in the Latta substitute, it would not necessarily have to stand, but this committee is going to have to find that $200 million somewhere, if not in this program. I think that is something that the committee has to consider. If in fact opponents are going to try to stop this procedure, where are you going to get the $200 million savings for the other programs the committee has jurisdiction over?

Thank you, Madam Chairman.

Ms. MIKULSKI. Thank you very much, Mr. Snyder.

We now recognize the chairman of the full committee, Hon. Walter Jones.

STATEMENT OF HON. WALTER B. JONES, CHAIRMAN, COMMITTEE ON MERCHANT MARINE AND FISHERIES

Mr. JONES. Madam Chairman, thank you very much.

We are again back on the CDS payback. As all of you know and this committee is aware, the original CDS payback rule is on the verge of being implemented.

Chairman Biaggi has called this hearing today to see if the maritime community can put aside its divisions and gather around some compromise on this issue. I commend him for his efforts. To further this process, he has introduced his bill as a possible vehicle of compromise.

Along that line, I, too, have offered a bill, H.R. 2550, as a possible compromise.

Madam Chairman, I would like to summarize it inasmuch as it was only released, I believe, yesterday or the day before.

First, its effective date—that is, the bill which I have introduced—is September 1, 1985. Until that time, the Secretary's CDS payback rule will be in effect. Any operator willing to apply between June 6 and September 1 to pay back in full within the year can do so and will be entitled to permanent privileges in the domestic trade.

Now after September 1, the bill, if approved and enacted, would continue the current law's 6-month waiver. However, an operator can keep getting automatic extensions of 6 months each unless the Secretary, following the hearing, upholds a protest by a Jones Act operator that the continued presence of the payback vessel constitutes unfair competition for the nonsubsidized vessels in the trade.

After 3 years of continuous operation in the domestic commerce by a subsidy-built vessel, the subsidy can be repaid in full to obtain permanent Jones Act privileges.

In conclusion, I also might add that I believe that, regardless of what the CDS payback rule is that is implemented, title XI should be available to those who pay back.

Madam Chairman, that briefly is an explanation of the bill which I have introduced. I yield back the balance of my time.

Ms. MIKULSKI. Thank you.

The Chair recognizes Mr. Lent for an opening statement.

STATEMENT OF HON. NORMAN F. LENT, A U.S. REPRESENTATIVE FROM THE STATE OF NEW YORK

Mr. LENT. Thank you, Madam Chairlady.

I am very pleased that Chairman Biaggi has scheduled this hearing on the difficult issue dealing with allowing tankers built with construction-differential subsidy to pay back all or part of the subsidy and then be able to operate in the protected domestic trade.

As you know, I have been a strong supporter of the concept of allowing the payback of CDS money to provide more economical tanker transportation of the Alaska North Slope oil to the lower 48

States, not to mention the employment of some of the Nation's most modern, efficient vessels.

After the years that our committee has been wrestling with this issue, which does not even include the years when it was being discussed downtown and in the courts, I think it is now time to put this issue behind us and move forward and proceed with the implementation of the administration's rule as originally promulgated more than 2 years ago. However, I am aware of the arguments which have been propounded by the domestic tanker operators and appreciate the need for a careful study of this complicated proposal and its impact on them.

I will be very pleased to hear testimony this morning on the two legislative initiatives which are before the subcommittee to see if it will be possible to develop a compromise through the legislative process that might enable a payback program to be put in place.

I hope that the witnesses today will address, with actual facts and figures, the possible impact of the rule as proposed or the alternative legislative proposals. We have passed the time when we can rely on generalizations. In order for our committee to consider legislation, we need detailed information that will enable us to prepare an appropriate measures.

I, for one, feel that the administration's proposal has been prepared carefully and am inclined to accept the background material put together by the Department of Transportation and MarAd. Therefore, if there is to be a legislative alternative to the proposed rule, it has to be based on facts and figures and not supposition and generality. The burden, I think, is on the domestic operators to make their case before the committee.

I want to just close by commending Chairman Biaggi for his continuing efforts to try to obtain agreement on this difficult matter. I was quite disappointed, as were many other members of the committee, with the end run the other day over in the Appropriations Committee. I had thought that all of the parties were going to try to work toward a compromise with us here in this committee, and I hope that this forum today will provide us with a basis upon which we can make an intelligent decision to either accept the rule or prepare some suitable legislative compromise.

Thank you, Madam Chairman.

Ms. Mikulski. Thank you very much.

Mr. Saxton, do you care to make a statement?

Mr. Saxton. No.

Ms. Mikulski. Mr. Shumway.

Mr. Shumway. No.

Ms. Mikulski. Mr. McKernan.

Mr. McKernan. No, Madam Chairman.

Ms. Mikulski. Well, that concludes our opening statements. Now we would like to proceed to our witnesses.

I ask unanimous consent that the following be placed in the hearing record:

One, the statement of Jesse M. Calhoon, the president of the National Marine Engineers' Beneficial Association.

The statement of Andrew N. Garbis, vice president of Cove Maritime Companies.

The statement of Crowley Maritime Corp.

The statement of John Ervin, executive vice president of Trinidad Corp.

The letter from Robert W. Carson, president of the Tanker Management, Inc., dated May 15, 1985.

Ms. Mikulski. Hearing no objection, so ordered.

[The material can be found at end of hearing.]

Ms. Mikulski. Now we would like to proceed to our witnesses. The Chair would like to welcome Mr. Matthew Scocozza. I believe the other people with you are accompanying you; is that correct?

Mr. Scocozza. Yes, ma'am.

Ms. Mikulski. You are most welcome, and we ask you to proceed with your remarks.

STATEMENT OF HON. MATTHEW V. SCOCOZZA, ASSISTANT SECRETARY FOR POLICY AND INTERNATIONAL AFFAIRS, DEPARTMENT OF TRANSPORTATION, ACCOMPANIED BY WARREN L. DEAN, ASSISTANT GENERAL COUNSEL FOR INTERNATIONAL LAW; PAUL L. MARX, ECONOMIST, OFFICE OF THE ASSISTANT SECRETARY FOR POLICY AND INTERNATIONAL AFFAIRS, OFFICE OF ECONOMICS; AND THOMAS E. MARCHESSAULT, ECONOMIST, OFFICE OF THE ASSISTANT SECRETARY FOR POLICY AND INTERNATIONAL AFFAIRS, OFFICE OF ECONOMICS

Mr. Scocozza. Thank you, Madam Chairman and members of the subcommittee.

I have here with me today Mr. Warren Dean, the assistant general counsel for international law of the Department of Transportation; Mr. Tom Marchessault, to my immediate left, from the Office of Policy at the Department of Transportation; and, to my far left, Mr. Paul Marx, of the Maritime Administration.

I am pleased to have the opportunity to testify before this subcommittee on the repayment of construction-differential subsidies. Given the complicated history of CDS repayment, I thought it might be helpful to summarize the background of this issue and then describe briefly the basis for the Department of Transportation's decision that CDS repayment should be allowed for a 1-year period.

I think we can all agree, Madam Chairman, that the uncertainties surrounding the total repayment of tanker vessels which existed from 1978 until May of this year created unnecessary hardship for all concerned. We hope that our final rule will eliminate this uncertainty and return the decision on CDS repayment to those most capable of making the decision, the operators of the vessels themselves, on terms that would ensure fair competition with unsubsidized operators.

Despite the governmental programs, construction subsidies, and operating subsidies to U.S. vessel owners, U.S. flag tankers operating in foreign trade have not been successful on the whole. Since the opening of the Trans-Alaska Pipeline System in 1977, however, the demand for suitable tanker tonnage generally has not been met by the Jones Act in the Alaska oil trade. Accordingly, MarAd has used its authority to grant temporary permission under section 506 of the Merchant Marine Act to allow CDS-built tankers, primarily

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very large crude carriers, VLCC's, to participate in this trade and has granted total repayment applications to two VLCC's. These actions have generated a significant amount of litigation and controversy.

Previous regulations governing the total repayment of CDS were set aside by the Court of Appeals for the District of Columbia in 1982. On January 31, 1983, the Department proposed a rule setting forth the policy which would allow any owner-operator of a tanker built with CDS to repay its subsidy and, consequently, obtain a permanent removal of domestic trading restrictions. The proposed rule applied to tankers only, but was not limited to any particular class or size.

The terms of repayment were intended to put the operators of those vessels on an equal, competitive basis with existing Jones Act vessels now operating in domestic trade, thereby avoiding any argument that CDS vessels would enjoy an unfair advantage over unsubsidized domestic operators.

About 150 comments were received. Because the rulemaking clearly involved a major and controversial maritime policy issue, we carefully reviewed the entire record in preparing the final rule that was issued on May 3 of this year.

The issue of CDS repayment has been considered by the Congress in the past. On March 3, 1983, my former deputy testified before this subcommittee in oversight hearings on the subject of CDS payback. Approximately 1 year later I appeared before this subcommittee in hearings on H.R. 5071, a bill to define the criteria and procedures for the permanent admission of CDS-built vessels in the domestic trade.

Finally, Congress, through a series of appropriations measures, prohibited the Department from enforcing any final rule authorizing the total repayment of CDS until May 15, of this year.

On May 3, 1985, the Department of Transportation issued a final rule effective June 6, allowing the unrestricted repayment of contruction-differential subsidies for a period of 1 year. In return, restrictions on access to the domestic coastwide trades for these vessels would be removed.

For some time it has been recognized that tankers built with CDS have not been able to compete successfully and profitably in the foreign trades where they were originally intended to operate. It has also become clear that relying solely upon unsubsidized tankers for the carriage of Alaskan crude oil to the contiguous 48 States imposes unnecessary cost on the economy of the Nation and keeps certain tankers active well beyond their normal economic life, past the point where they provide efficient, cost-effective service.

We issued this final rule after careful, thorough, and lengthy review of all the options available to us, including maintaining the status quo. We are convinced that offering the opportunity for unrestricted CDS payment, while not without certain adverse impacts, will increase competition in the Alaska oil trade, will eliminate the distortions and uncertainties that often accompany Government attempts to regulate marketplace decisionmaking, and will ultimately result in a more efficient domestic tanker fleet that more fully meets the goals of the Merchant Marine Act of 1936.

The implementation of this rule will allow the fullest use in the domestic trades of the most efficient U.S.-built, U.S.-owned, and U.S.-crewed vessels available. These large tankers carry crude at a lower cost per barrel than do small tankers, simply because vessel operating costs do not increase proportionately as cargo volume increases. Our analysis is based upon the proposition that the main factors ultimately determining which tankers serve each market are a combination of economies of tanker size, length of voyage, tanker operating costs, size restrictions, and the quantity of Alaskan crude demand at specific ports.

On the basis of these operating and demand characteristics, CDS repayment will result in the displacement of higher-cost vessels by lower-cost vessels. The total cost of transporting Alaska oil to the contiguous United States will be significantly lower if tanker owners are allowed to fully repay their outstanding CDS plus compounded interest in return for unrestricted access to the Jones Act crude oil trades.

The savings to the economy from this improvement in the shipping efficiency could total over $800 million, net present value over the next 10 years. The lower transportation costs could increase demand for tankers in the trade, as oil companies are abel to increase their shipments to gulf coast ports.

The opportunity for unrestricted repayment is limited to a 1-year window in order to allow time for repayment to be completed while limiting the period of uncertainty for ship operators and shipyards in which vessels will choose to repay.

The full-time use of CDS-built tankers will principally diminish the employment opportunities of the smallest, oldest, and least efficient tankers in the Alaska oil trades, although initially there may also be employment problems for some larger tankers currently active in the Alaskan oil trades.

We realize there may be some title XI defaults as a result of permanent use of the VLCC's, but we have every reason to believe that the Federal receipts from CDS repayment will more than offset any losses that do occur. On the other hand, the elimination of the current uncertainty about the use of VLCC's will make it easier for oil companies and tanker owners to plan for future oil traffic.

In summary, while not without certain negative consequences, allowing unrestricted CDS repayment will generate greater net benefits to the Nation than either maintaining the status quo or adopting any other option available to the Department.

We have received copies of two legislative proposals in CDS repayment. One is a bill that has been introduced as H.R. 2550, and the second has already been introduced as H.R. 2485. I would like to comment on both bills.

The first bill we received would allow CDS-built vessels entering into the domestic coastwide trades without a limit of 6 months per year, so long as no vessel which has not reached the end of its economic life were displaced.

After 3 years of uninterrupted, temporary access, the owner of that tanker would have to decide at that point whether to fully repay.

The second bill, H.R. 2485, would allow owners of tankers built with CDS to repay one-half of their unamortized CDS plus interest in return for entry into the domestic Jones Act trades every other year.

The most positive aspect of the first bill is its implicit recognition that it is highly desirable to allow CDS-built vessels into the domestic trades for periods of more than 6 months out of the year.

Another positive aspect is its explicit notice that old, obsolete, inefficient vessels should not be allowed to preclude the use of the more efficient CDS-built VLCC's. However, we are concerned that the bill seems to maintain and even extend what we are convinced is a questionable premise—namely, that the Government must regulate the amount of capacity in the domestic trades, despite the inefficiencies, excessive costs, and market distortions that a regulatory approach engenders.

If this bill were enacted, it would eliminate virtually all of the immediate benefits identified for unrestricted payment, including the immediate receipt of unamortized CDS repayment plus interest, the immediate realization of transportation savings that will——

Ms. Mikulsi. Mr. Scocozza, excuse me. Could you summarize your critique of those two bills, so that we can move on to the questions?

Mr. Scocozza. Well, I am just about finished with my testimony. But, quite simply stated, Madam Chairman, the Department of Transportation at this time sees positive aspects about the bills, what moved them, the recognition that obsolete vessels should not be protected.

But our position is that, on the basis of all the information, all the research that we have done, we believe the rule as proposed should be the only remedy available to tankers desirous of entering into the trades.

We think the 1-year in, 1-year out is actually less attractive to VLCC owners than the existing status quo of 6 months in and 6 months out.

The other bill, which requires 6 months in and a 3-year waiting period, the question is whether or not 2½ years into the exercise a 100,000 deadweight ton vessel might be displaced and the running time would stop.

In short, Madam Chairman, I think credit is owed to the authors of these pieces of legislation, but the Department of Transportation at this time would not be prepared to support either one, as opposed to the rule that we have promulgated.

I would be glad to respond to any questions that you or the other members of the subcommittee would have at this time.

[The remainder of prepared statement follows:]

Remainder of Mr. Scocozza's Prepared Statement

. . . result from the implementation of our rule, and the timely elimination of the uncertainty that has been a characteristic of the Alaska oil trade in recent years.

This draft bill continues, and even extends, one of the objectionable aspects of the system before we issued this final rule, i.e., that access to the domestic trades must be denied to CBS-built vessels if that entry would prejudice the competitive position of non-CDS-built vessels. Under the current system, a CDS vessel is denied temporary access if any vessel over 100,000 deadweight tons is idle; under the draft bill, access would be denied if any vessel under 20 years old is idle. This would encourage the use of older, less efficient vessels, maintaining the high cost of transporting Alaskan crude oil. Moreover, the bill would seem to encourage owners with a mix of both older and younger vessels to use their older tankers so that the idleness of their newer vessels will "block" the use of CDS-built vessels. To us, this seems to be a dubious approach to promoting an efficient merchant marine, that has not worked well in the past.

The second bill under discussion also appears to recognize that the current regulatory system has not been satisfactory and that it should be changed. We do not believe that the system proposed by this draft bill will materially improve the transportation of Alaska North Slope crude oil. Essentially, this bill continues the present system of "half in/half out" for the CDS-built tankers. The only change is the time period. Under the current system, the base period is one year; under this proposal it would be two years. The end result would still be a practice of not fully utilizing the most efficient tankers.

The individual owner of a CDS-built tanker may be no better off under this proposed system than under the existing system of temporary permissions; however, if the proposed bill were enacted, the vessel owner would be required to make a substantial, up-front investment in order to continue with what are still temporary permissions to enter the domestic trades.

Finally, we do not believe that the use of CDS repayment receipts should be earmarked for additional construction subsidies. We have testified in the past that the use of ship construction subsidies has not been successful. The Administration has not sought funding for construction subsidies and we continue to oppose efforts to reinstate them.

IV. CONCLUSION

For the reasons cited above, the Administration strongly opposes enactment of these proposed bills.

Mr. Chairman, we issued this CDS repayment rule after long and thoughtful consideration of all the interests potentially affected. We did so in the belief that the approach decided upon would ultimately result in a more efficient marine transportation system and would remove the federal government from an area where our interference has neither helped the needs of shippers nor improved the viability of the domestic merchant marine. Our approach should also reduce economic pressures to export Alaska North Slope oil, which would have a very detrimental effect on the merchant marine as a whole.

In closing, I want to emphasize that there is nothing in the final rule we issued that *mandates* repayment and entry into the domestic trades. Additionally, there is nothing to preclude the parties in this segment of the industry from making whatever arrangement they believe is beneficial to the individual interests of the affected parties (subject, of course, to the same antitrust requirements that limit the actions of other U.S. companies).

Thank you, Mr. Chairman. I am prepared to answer any questions you or other Members of the Subcommittee might have.

Ms. MIKULSKI. Thank you very much for your testimony. I look forward to our conversations on it.

As someone who represents a maritime community, it is my goal to hope that we can protect the integrity of the Jones Act, the investment climate for domestic ship construction, the maximum amount of seafaring jobs, and our Nation's sealift capacity. Therefore, some of the questions that I want to ask you are these:

I thought that Congress was very clear when it passed the Merchant Marine Act of 1970 in what it wanted in terms of tankers and why it would be used in foreign commerce.

What I am surprised at is how we got into this rulemaking process to begin with. Under what authority do you think you have the right to alter congressional intent through a rulemaking process in which you held no public hearings?

Mr. SCOCOZZA. Madam Chairman, there were hearings on the individual—excuse me. There was a tremendous amount of comments, over 150 different individual comments that were filed on the record, which is a very, very long process that has gone on. It has been the subject of court battles. There has been a tremendous amount of opportunity for the public to submit their comments before the Department of Transportation. Witness the fact that we have been here in oversight hearings on three different occasions on this very thing.

With respect to the merchant marine——

Ms. **Mikulski**. Excuse me, Mr. Scocozza. We held hearings because you didn't.

Mr. **Scocozza**. Yes, ma'am; and we participated.

I would also say, Madam Chairman, on the basis of the Act of 1936 as amended, I think the rule complements it because what it is doing, its objective is to foster the safest, the best equipped, and the most efficient tanker fleet in that particular Jones Act trade. I think the preamble to the rule sets out the manner in which we believe it complements the Merchant Marine Act of 1936.

Ms. **Mikulski**. Well, one of the arguments which has been made is that the Federal Government would get revenue, as much as $277 million, for virtually no investment. That looks like a pretty good deal for the Federal Government. However, the Department, in its rulemaking, indicates that the defaults in the title XI loans as a result of the Jones Act tankers displaced by the rule could reduce this windfall by over one-half.

I have a study done by a firm called Deloitte, Haskins & Sells that talks about the impact on the Treasury of this rule. It indicates that the rulemaking will have a negative impact on the Treasury, as much as $477 million by 1990. It suggests as many as 8,000 jobs in the shipbuilding and seafaring industries, as well as jobs from the multiplier effect of these industries, could also be lost.

How did you make your calculations about the cost-benefit ratio on this rule, and how do you account for the wide disparity between your figures and the Deloitte, Haskins & Sells study? They are pretty big gaps.

Mr. **Scocozza**. Madam Chairman, I must be very honest and admit that I am not familiar with that individual study, but I am familiar with the 71-page economic analysis that accompanied the rule.

We do estimate that there could be perhaps as much as an 800-person displacement; 8,000 jobs is a new figure. There has to be some kind of reason for that kind of disparity.

The $450 million adverse impact on the U.S. Treasury is another number that is new to me. The $170 million is our best guesstimate of potential title XI defaults as a result of this rule. That is correct as you have stated.

But the other thing, Madam Chairman, is that we did not do this just simply to create revenues for the Federal Treasury. That transcends all of the testimony previously before this subcommittee. We are looking at trying to promote and develop the safest, most efficient tanker fleet that we can. That is a principal objective.

Certainly the fact that there is going to be $277 million returned to the Federal Treasury is nothing to handle lightly, but that is not the controlling factor.

Ms. **Mikulski**. Well, we have some differences here. Rather than pursue questioning on a study you have not seen, what I would like to do in expediting the committee's work is pass this on to you, have you take a look at it, and if you could account for the differences, I would like you to do so before the rule takes effect. It is very simple and straightforward, and it really does give me enormous pause to have such a disparity in conclusions. (Nothing was received in reference to the above at time of printing.)

One of the other concerns I have is about national security. The argument has been made that most of the tankers which would be displaced are rust-bucket types anyway and would not have any significant military use. Well, my reading says that this is not true. Since the initial rule was proposed in 1983, the number of Jones Act tankers which have been scrapped is on the order of two and a half ships a month. So old ships are kind of out now.

In addition, some companies would suffer from this rule like American Trading Transportation Co. of Baltimore. ATT's ships are only 3 years old. That is younger than my American-built car. I would imagine maybe it is as efficient, if not more so.

Having said all this, would you agree that the kind of ships being displaced are smaller tankers around the 50,000 deadweight class which are often really used by the military? That the military doesn't normally use the very large carriers? And that this rule could have a strong negative impact on our national security and American merchant marine ships necessary to back up Secretary Lehman's 600-ship Navy, if we need to?

Mr. **Scocozza**. Madam Chairman, I would say that you are right; that there would probably be a larger impact on the smaller than 100,000 deadweight ton vessels, but I would like to make a comment on the actual operation of the trade between the North Slope and the lower 48 and the Panama Canal.

By virtue of the size of some of the ports where the vessels are serving, a VLCC is an inappropriate vessel. There are markets where these types of vessels are most appropriate.

Now in this particular situation, if the VLCC's come into the trade, there is going to be a movement, there is going to be a transition of different ships in different particular markets, different ports, as a result of the influx of these more efficient carriers.

The thing that I think will happen is the most efficient of these smaller vessels are going to survive. The ones that may be having a competitive disadvantage, because there might be a rust-bucket with no debt service on it, putting a 50,000 deadweight ton vessel that is more efficient and more consistent with national security goals out of a market might have a better chance, because it can be more efficient in these smaller particular ports.

I follow your rationale about the importance of national security. We have, in fact, paid a tremendous amount of attention to that and have dealt with that in our analysis that accompanied the rule.

But I think the end result will be that all of the vessels that will survive, the smaller vessels that are important for national security, will get a more guaranteed future because the competition in the smaller ports will be much higher, and I think they will do a much better job.

Ms. **Mikulski**. While our chairman is getting updated, I will just ask one more question.

How many of these handy-sized tankers do you actually think we need for sealift purposes and how many are available from the U.S. merchant marine?

Mr. **Scocozza**. Madam Chairman, I don't have those statistics available immediately. I would be delighted to provide that.

[Information to be provided follows:]

Tanker Needs for Sealift Purposes

The vessels that the Navy Department considers to be "militarily-useful" for sealift purposes are those vessels under 80,000 deadweight tons and with coated tanks. As of October, 1984 there were 114 U.S.-flag tankers in that category.

The Office of the Secretary of Defense is just completing a new study of the maritime sealift requirements for tankers, and the information you request is not yet available. The study will define the need for what are termed "military usable" tankers and, as a subset of that, the need for "handy-sized" tankers, which are defined as able to carry 200,000 barrels of petroleum. The Department of Defense indicated to us that this study will be available from their Office of Program Analysis and Evaluation in the near future.

Mr. **Scocozza**. There is some element of the national security question involved there. If that is the case, I would be glad to provide that to you, to the committee, on a classified basis.

Ms. **Mikulski**. I understand that.

This committee, under Mr. Biaggi, held extensive hearings a term ago on our sealift capacity. I think that in an unclassified way the unclassified information would reveal about 160 ships. We also know that a lot of the effective U.S. control fleet ships are principally those of Liberia and Panama. That gives me a great deal of concern because Liberia—particularly Liberia—I do not think can be viewed as an ally of the United States. For example, in the Arab-Israeli War, they explicitly told people not to help Israel. I would have a feeling that they could be told not to help us.

My concern about your rulemaking is that it will really have a terrible adverse effect on the American shipbuilding industry, changing the rules of the game for good guys who built with no subsidies to do Jones Act trading and I think it is going to cost us jobs and really soften our military readiness. But this is just one committee member's opinion, and I would be happy to turn to Mr. Snyder for questioning and relinquish the Chair to the chairman.

Thank you.

Mr. **Scocozza**. Thank you. We will be glad to respond to the questions that you have, Madam Chairman.

Mr. **Snyder**. Thank you, Madam Chairman.

Mr. Secretary, maybe Mr. Dean can help us with this. I think he is your lawyer down there.

The language that was affixed to the appropriations bill in committee the other day, you are familiar with that?

Mr. **Dean**. Unfortunately, Congressman, I have not seen the actual text yet.

Mr. **Snyder**. Well, let me read it to you. Maybe we will run a copy down there to you.

It is:

> None of the funds provided in this or any other act shall be used for the enforcement—my emphasis—of any rule with respect to the repayment of construction-dif-

ferential subsidy for the permanent release of vessels from restrictions in section 506 of the Merchant Marine Act of 1916 as amended: Provided such funds may be used to the extent such expenditure relates to a rule which conforms to statutory standards hereafter enacted by Congress.

My question is, what action would you be taking that would be enforcement as opposed to implementation? You wouldn't intend to enforce this on somebody; payback is strictly voluntary on their part, isn't it?

Mr. SCOCOZZA. I would imagine that any problem with that amendment could be fixed with a technical amendment, Mr. Chairman, by the full committee on the floor.

The point that you are making is right—it is not the enforcement; it is the implementation of the rule. We could be prevented from implementing the rule by saying none of the funds shall be used for salaries to implement the rule.

It may also be subject to a point of order because it says "any other act," and it has been a long time since I worked in the House, but that seems like it is legislation in an appropriations bill and perhaps may be subject to a point of order.

Mr. SNYDER. Unless they get a rule.

Mr. SCOCOZZA. But it certainly could be a limitation in an appropriations bill to at least be effective for the length of the supplemental through September 30. For all practical purposes, it could be fixed to work and not subject to attack until October 1.

Mr. SNYDER. What would be your reaction to an application for payback if Congress has not enacted this by June 6?

Mr. DEAN. Had not enacted this?

Mr. SNYDER. Yes; this is just out of committee. I don't know when it is scheduled for floor action, but the story around here is that we may not have a heavy legislative agenda next week. We will be back here on whatever the Tuesday after that is, something like June 4.

Your rule takes effect June 6, if I am not mistaken. If you had an application lying there on June 6 and the supplemental had not been enacted, you would be in a position to go ahead and approve that?

Mr. SCOCOZZA. We would be in a position to grant individual applications starting June 6, if in fact the application satisfied all the criteria set out in the rule and the appropriate financial considerations were satisfied. It would probably not be enacted, the restriction on us would probably not be enacted into law and would probably not occur before—you would be a better judge than I, Congressman. The soonest that the President would sign that——

Mr. SNYDER. Well, I don't know, but assuming that we get it that week, obviously it is going to take a little while for it to go through the other body and downtown.

I was just interested in what your reaction would be assuming that it was not law by June 6.

Mr. SCOCOZZA. The indications that we have are that such an amendment would not be in a Senate appropriations bill at this particular time, and it would be the subject of a conference and maybe a protracted argument over the issue.

Mr. Snyder. Is it safe for me to assume, then, you would probably go ahead and proceed, provided this has not been enacted into law by June 6?

Mr. Scocozza. Yes, Congressman.

Mr. Snyder. I guess for the record, rather than asking you right now, would you describe for us—and perhaps it is in your study—exactly which ships and how much money might be in danger of default under title XI?

Mr. Scocozza. We can do that for you.

[Material to be supplied follows:]

TITLE XI LIABILITY

As discussed in detail in the Regulatory Impact Analysis, our assessment of the possible Title XI liability as a result of this rule is that it could be as high as $170 million.

Two existing VLCCs currently in the trade (the *Bay Ridge* and the *Stuyvesant*) may be unable to support their very high mortgage obligations of about $108 million; it is expected that the government will recoup all of this amount from the sale of the vessels. In addition, there is the possibility that one or two vessels under 20 years old between 100,000 DWT and 140,000 DWT might experience difficulty finding employment, at least initially, and might choose to default. We estimated that the total default would be, at most, $70 million, and that much of this would be recouped from the sale of the vessels. It is uncertain which vessels these might be but the tankers operating in the ANS trade that are under 20 years old and in this size range are the following:

[Dollar amounts in millions]

	Year built	Title XI as of Dec. 1, 1985
Vessels:		
Arco Anchorage	1973	
Arco Fairbanks	1974	
Arco Juneau	1974	
Kenai	1979	$39.4
Mobil Arctic	1972	
Overseas Boston	1974/1981	28.1
Overseas Juneau	1973	17.3
Prince William Sound	1975	
Tonsina	1978	42.9

Mr. Snyder. Madam Chairman, I think we ought to move along. I ask unanimous consent to submit more questions.

Mr. Biaggi. "Madam Chairman" has converted. [Laughter.]

Mr. Snyder. Medical science is wonderful!

Mr. Biaggi. Without objection, so ordered.

[Questions and answers to be supplied follow:]

QUESTIONS SUBMITTED BY CONGRESSMAN GENE SNYDER AND RESPONSES BY MATTHEW V. SCOCOZZA

Question. The Secretary's new rule governing repayment of construction differential subsidy (CDS) and permanent admission into the coastwise trade for tankers contemplates that all seven CDS VLCC's will repay. What is the fiscal impact if all seven VLCC's do not in fact repay, generally, and if the three Seatrain vessels, particularly, do not repay?

Answer. We anticipate that all seven VLCC's will choose to repay. However, the table below shows the estimated CDS repayment for each of these vessels. If the

Seatrain VLCC's do not repay, we estimate that federal receipts from CDS repayment would be approximately $146 million.

Vessel names (owner):	*CDS repayment*
Arco Independence (Atlantic Richfield)	$44.4
Arco Spirit (Atlantic Richfield)	$43.5
Maryland (Seatrain)	$42.8
Massachusetts (Seatrain)	$45.1
New York (Seatrain)	$42.8
Williamsburgh (Petrofina)	$37.1
Brooklyn (Petrofina)	$21.0

Question. The new law and regulations governing the approval of Title XI guarantees contemplates an "economic soundness" criterion for approval, including the effect which issuance of the guarantee might have on overtonnaging in a given trade. Arguably, at least according to the rule's opponents, the Alaska north slope oil trade is already overtonnaged, as witnessed by the vessels that are in layup or have been scrapped.

A. If that is true, does the Department now have the authority to issue Title XI guarantees to facilitate a payback by any of the CDS-built tankers?

B. If Title XI guarantees were not allowed, what would be the impacts upon the fiscal benefits anticipated from implementation of the rule, particularly involving Seatrain—both the three vessels projected to repay and the two already in the trade?

Answer A. The requirement to consider the effect of overtonnaging in a given trade does not preclude the Department from approving a Title XI loan application if there are vessels in layup or if vessels have been scrapped. The purpose of that provision is to determine whether there are vessels already operating in the trade that would adversely affect the competitive viability of the applicant's proposed vessel and, thereby, increase the likelihood of Title XI default.

B. If Title XI were not allowed for CDS repayment, Seatrain's management has stated that they would be unable to repay their outstanding CDS obligations on three vessels. In that case, the total amount of CDS repayment would be about $146 million. If only four vessels repaid their outstanding CDS obligations, the impact on the existing Seatrain Jones Act vessels (*Bay Ridge* and *Stuyvesant*) is uncertain. Whether the CDS-built Seatrain vessels that operate outside the domestic trades could continue to earn sufficient revenues to avoid default is speculative, since they have $87.5 million in outstanding Title XI balances.

Question. A legislative compromise to the DOT rule has been suggested wherein only one CDS-built vessel per operator might be permanently admitted to the ANS oil trade.

A. What would be the fiscal impacts arising from implementation of that proposal? What about the suggestion that only VLCC's be permitted to repay?

B. What is the Administration's position on either of those alternatives?

Answer A. If only one vessel from each company were allowed to repay its CDS, the amount returned to the Treasury would, first, depend upon whether tanker owners could avoid that prohibition. For example, it is common in the tanker industry for there to be several one-vessel companies that are actually owned or affiliated with a particular parent company. In addition, unless it were specifically prohibited, a company could sell its non-eligible vessels to another party who could then repay the CDS and enter the domestic trades. There are, undoubtedly, many other ways that such a limitation could be circumvented. In any case, if the necessary language could be devised to avoid such an eventuality, the amount of CDS (plus interest) for the VLCC's would be $107 million. If the Panamax vessels repaid their outstanding CDS obligations an additional $31 million would be recovered.

Our analysis concluded that, for the most part, it would only be profitable for the VLCC's to repay their outstanding CDS obligations; therefore, any legislation which limits repayment to VLCC's would result in the $277 million in repayments, the sum we estimated in our Regulatory Impact Analysis.

B. The Administration opposes any attempt to overturn the Final CDS Rule just issued by the Department of Transportation. The Department considered each option carefully but finally concluded that unrestricted CDS repayment resulted in the most net benefits to the Nation and did the most to improve the overall efficiency and long-term competitive viability of the domestic merchant marine.

Mr. BIAGGI. Mr. Jones.

Mr. JONES. Thank you, Mr. Chairman.

I have one or two questions for the Secretary, if I might.

According to your testimony regarding H.R. 2550, I assume that your statement was contrived from a draft which you saw, not the bill itself?

Mr. **Scocozza**. That is right, Congressman. We had just learned today that it was filed.

Mr. **Jones**. Let me go one step further. Does the delay of the effective date of H.R. 2550, as introduced—could it possibly alter the Department's position?

Mr. **Scocozza**. Congressman, that is a positive aspect of the bill from our perspective. Once again, we have to look at the situation.

If in fact this amendment is successful in the appropriations bill and your bill were enacted, we may only have a 2-week period of grace, because the period in your bill would run simultaneously with the length of the supplemental appropriations bill. So it would actually defeat the purposes of the provision that you had put in there.

The other thing, Congressman, is that we felt very strongly that decision had to be resolved once and for all for all of the carriers in the trade. If the opportunity for 5, or 6, or 7 years out were still that people could be paying back completely, it would have an impact on future planning and future construction and development of equipment by individual carriers.

Mr. **Jones**. Looking at the other side of the coin, doesn't the effective date of September 1 actually permit the payment of the entire $277 million in the next fiscal year if that money is available? There is nothing in H.R. 2550 to prohibit, prior to September 1, any company, or shipbuilding company, operator, to fully pay back.

Mr. **Scocozza**. That is right, Congressman, but I make the observation that, if the appropriations bill is successful, there will not be any grace period; there will not be any payback other than perhaps a week or two in June.

Mr. **Jones**. That isn't before us here this morning—the appropriations bill. That is down the line somewhere.

Mr. **Scocozza**. Sure.

Mr. **Jones**. What is before us is this implementation of CDS payback.

Mr. **Scocozza**. Another observation and comment I would make, Congressman, is that a 6-month opening and then stopping it right there is probably a more productive thing in terms of the way the Department would look at it, because it would be decided with a degree of finality that there would be no more complete paybacks after that particular date. That is why we like the window, the rule that we have that just says you will have 1 year to buy back and that is it, and then it is the status quo.

Mr. **Biaggi**. Would the chairman yield?

Mr. **Jones**. I yield.

Mr. **Biaggi**. On that point, what is to say that the following year another attempt will not be made to extend the rule?

Mr. **Scocozza**. Congressman, I could not guarantee that by a successor agency or administration, but that is not our plan.

Mr. **Biaggi**. That is not your plan today.

Mr. **Scocozza**. I know, Congressman; your point is well taken. A rule can always be amended or extended.

Mr. **Biaggi**. Thank you.

Mr. **Scocozza**. Once again, that is not our desire.

Mr. **Jones**. One final word, to try to put this thing in perspective: the CDS payback ball is now in your court obviously, due to the rule which goes into effect June 6. What we are trying to do, those of us who are trying to look at both sides, the pro's and the con's, is to come up with some reasonable compromise with which most people can live.

Now whether H.R. 2550 does that or not, at least that was the intention in introducting that particular bill. I am a little surprised that the Department could not take a little more charitable view of it in the spirit of compromise, but, nevertheless, I don't run the Department; I am not a part of it.

One final question: what is the position of the Department on the availability, the use, of title XI funds in connection with these transactions?

Mr. **Scocozza**. Congressman, as I have mentioned in the detailed statement that I will submit today, the statute allows it, and we don't have the discretion to not look at that exercise at all.

We have toughened the criteria for title XI loan guarantees with 25-percent money upfront instead of 12.5 percent, but because the statute does allow it for this particular purpose, and that has been recognized by the courts, we will consider applications to use title XI funds for this purpose.

Mr. **Biaggi**. Will the gentleman yield?

Mr. **Jones**. I yield back the balance of my time. I have no further questions, Mr. Secretary. Thank you very much.

Mr. **Scocozza**. Thank you, Mr. Chairman.

Mr. **Biaggi**. On that point, given the condition of the title XI fund, do you think it would be advisable to use those funds for this purpose, whether it be 12.5 or 25 percent?

Mr. **Scocozza**. I think, Mr. Chairman, it would depend on the individual application that was filed before the Department of Transportation. But the question is a very well-placed one because of the size of the title XI loan guarantees.

Because of the statute, it is an appropriate use of title XI. I guess the question goes much broader. We have to look at the whole trade, the tremendous amount of benefits that we see to the shipping community as well as the health and vitality of the trade. Looking at all these tradeoffs and looking at the amount of revenues that will be coming into the Federal Treasury, in spite of the fact that title XI will hurt, we opted on the side of issuing the rule.

Mr. **Biaggi**. Let's stay with what title XI permits. We understand that the law makes these applications eligible. Evidently, it made an awful lot of applications eligible in the past; and loan guarantees were issued that put title XI in the calamitous situation we find it. The use of that fund is being severely curtailed, notwithstanding the provision of the law permitting it.

I hope the Secretary is aware of the present condition of the fund.

Mr. **Scocozza**. She is.

Mr. **Biaggi**. It is in extremis. We will have to go to the Treasury for additional moneys. Also, its impact on the industry in the gulf has been devastating. Although it was permissible by law, it was poor administration and judgment.

It was a fund that was exploited and abused, although well intended. So it would seem to me that, given the present curtailing attitude of the Maritime Administration, that to bring other applicants in within the scope of title XI would not be very prudent. It is exactly what this committee is reviewing, with the possibility of dealing with it in a legislative fashion.

Mr. **Scocozza**. I appreciate the point that you are making, Mr. Chairman, but in your deliberations I hope you will look at the rule in the context of how we have tightened it up, to insure that, if ever again loan guarantees are given to an individual company, they have to meet a much higher standard than companies in the past.

I would certainly predict that the amount of loan guarantees that are expended in the future would be dealt with in a much more strict fashion than had been done in the past, but the statute is still there.

I think the main change that has occurred is the upfront money, from 12.5 to 25 percent. We are not looking at title XI to save companies, but basically to strengthen and enhance companies that have a future, companies that indicate that they have positive, new opportunities to exploit and need the title XI guarantees to expand.

People have told me that title XI money is not real money, and I argue with that because it is real money. The money that we have to pay in when there is a default is absolutely very real money. So I don't want to mislead the subcommittee in saying, "Well, it is just a little loan guarantee. It is like cosigning a note." If your son or daughter does not make the car payments, you have to pay for the car. It is a very real and very serious responsibility we have at the Department, and we take it that way.

Mr. **Biaggi**. Thank you.

Mr. Snyder.

Mr. **Snyder**. That recent MarAd rule, though, requires a finding of economically sound operation before you can make the commitment.

Mr. **Scocozza**. That is right, Congressman.

Mr. **Biaggi**. Mr. Lent.

Mr. **Lent**. Thank you, Mr. Chairman.

I would like to just touch on two of the issues that have been brought up earlier. Ms. Mikulski talked a little bit about the effect of this rule on the Navy. In the testimony of the president of the National Marine Engineers' Beneficial Association, which was submitted today, the point is made that if these overaged tankers are of any military importance, which some do contest, then the prudent course is not to run them to the end of their structural life, at which point they are of no use to anyone, but to purchase them now on a phased basis for the Reserve Fleet, so that CDS payback thus could help prolong the life of these tankers very significantly; is that correct?

Mr. **Scocozza**. That is, Congressman.

Mr. Lent. You make the point in your testimony that if we can use these larger tankers carrying the crude, it will be at a much lower cost per barrel than do the small tankers, because the vessel operating costs would be lower and they do not increase proportionately as cargo volume increases.

I represent a district—and I know other members of the committee do—on the northeast coast where many of their constituents use home heating oil. I think 85 percent of the homes in my district use home heating oil. As a consumer advocate, I would be interested in getting some idea if the DOT made any kind of an analysis of what these savings might translate into on the east coast in terms of home heating oil, or gasoline, or whatever. Was there any kind of an analysis done?

Mr. Scocozza. We have estimated that the savings and the efficiencies would result between $800 million and $3.2 billion over the next 10 years, depending upon the price of the oil at the wellhead.

The question with respect to how it would impact right at the pump, right before it goes into an automobile, is something that I don't believe we have specifically, but we can try to highlight it in our analysis for you and give you whatever we do have at the Department in that regard.

Mr. Lent. Well, I would appreciate it if the record could be held open, because I don't know how $800 million to $3.2 billion in savings translates into at-the-pump cost for the average homeowner in the Northeast.

[Material to be supplied follows:]

Regulatory Impact Analysis

Our Regulatory Impact Analysis did not claim any particular benefit to consumers, but simply estimated the benefits to the economy without attempting to determine to whom they would accrue. Our estimate of the transportation savings on crude oil shipped from Valdez to the Gulf and East Coasts is approximately $1.33 a barrel (about 3.2¢ per gallon). The actual price that consumers pay for heating oil and gasoline is determined by many factors including the base price of oil, the cost of refining, the price of competing fuels, the price elasticity of demand, as well as the cost of transportation. We did not attempt to determine how much, if any, of the transportation savings would accrue to consumers.

Mr. Scocozza. I would make an observation, Congressman, that the North Slope oil is approximately 14 percent of domestic consumption. The $800 million to $3.2 billion would be spread over 14 percent of the consumption in the United States.

Mr. Lent. Thank you, Mr. Secretary. I have no further questions at this time.

Mr. Biaggi. Mr. Anderson, do you have any questions?

Mr. Anderson. No.

Mr. Biaggi. Mr. McKernan.

Mr. McKernan. Thank you, Mr. Chairman.

Mr. Secretary, it is my understanding that under existing regulations there can be a waiver granted to allow CDS payback. What happens to those funds when that happens?

Mr. Scocozza. Those funds are put in the General Treasury, Congressman. You are correct; there are about 6 VLCC's that have been given consistent 6-month waivers; 3 are in for 6 months, then they are out; 3 more are in for 6 months. Consistently over the past several years there has been the equivalent of three ships in, but they have been trading off.

Mr. McKernan. What would happen to the funds derived from allowing CDS payback under your new rule?

Mr. Scocozza. Into the General Treasury, and that relates to a question that I answered of the chairman, when he pointed out that it would impact adversely the title XI exposure and the title XI situation. The point I make here is that the Federal Government, the amount of revenues that are coming in would be offset.

Mr. McKernan. Just procedurally, could you explain what happens if funds are not available in title XI to make the payments? Where do you get the funds that would be necessary?

Mr. Scocozza. In the case of a default, we have to borrow from the Treasury.

Mr. McKernan. You have to borrow from the Treasury?

Mr. Scocozza. And the fund is exhausted; we would have to borrow from the Treasury.

Mr. McKernan. Have you given any thought to try to earmark these funds to go for either title XI defaults or any other type of program that might benefit the maritime industry?

Mr. Scocozza. That would require a legislative change. In the process of our rulemaking, it was not within our jurisdiction to do that.

Mr. McKernan. I understand that, but do you have any comment on whether that would be something that you would at least entertain? I realize you are not going to give me a straight yes or no right here.

Mr. Scocozza. I would say, as a policy person at the Department of Transportation, I would probably say, no, Congressman, because I think the title XI program has not been what we all had wanted it to be. I think this might be perpetuating title XI. Perhaps there will be a successor program to it someday; I don't know.

We opted—our position right now would be to opt for the money going back into the General Treasury and to keep title XI as it is and deal with it specifically.

Mr. McKernan. You would not support using the funds for any other type of program such as a reengining program or something like that to try to help some of the present competitors to have a better opportunity to compete?

Mr. Scocozza. That is something that we would not be prepared to do right now.

Mr. McKernan. I have no further questions. Thank you, Mr. Chairman.

Mr. Biaggi. Mr. Secretary, you oppose both bills. Could the administration support any approach other than the rulemaking?

Mr. Scocozza. It would be impossible for me to say no, Congressman, because everything is possible in the world. But I would say at this particular time, looking at the possibilities, the timing, the fact that a lot of carriers have been waiting a very, very long time, this comment period has been open since May 1983, that we feel that the rulemaking that is before us now, the opportunity we have on June 6 is the best as far as the administration is concerned and all the interested parties that came before us.

Mr. **Biaggi**. The rulemaking states that no Panamax-size vessels will pay back CDS. Yet, we have witnesses here who intend to pay back their subsidies. Please comment. Also, what impact would this additional tonnage have on the domestic trade?

Mr. **Scocozza**. I am a little hard of hearing, Congressman. Did you say that no Panamax vessel could pay back?

Mr. **Biaggi**. No. The rulemaking assumes no Panamax-sized vessels will pay back CDS.

Mr. **Scocozza**. We don't expect Panamax vessels to pay back, but they would be allowed to if they chose. They would qualify to pay back. But at this particular time we don't believe any will. Perhaps the witnesses will correct me if I am wrong.

Mr. **Biaggi**. What impact would this additional tonnage have on domestic trade?

Mr. **Scocozza**. In the analysis that we have done, the 71-page analysis, we have indicated that we believe, if the Panamax vessels paid back, their costs for providing Alaska North Slope service would be much higher than the competitors in the trade. In other words, if they got in, they would probably be forced out by the Jones Act market, because their costs would be much higher.

We have some statistics on debt per 1,000 deadweight tons. It shows that the VLCC's, when they paid back their CDS plus their compounded interest, would probably have the level of debt service comparable to the efficient carriers in the Jones Act. If the Panamax vessels paid back, their debt service would be higher. I don't think they would be able to compete as well for the market as even the inefficient carriers, but that would have to be a consideration that a company would make before they bought in.

Mr. **Biaggi**. When you talk about increase of the financial factor and the contemplation of the cost, isn't the extra size, the extra capacity to carry, isn't that compensating? Does that balance off in the cost factor, so they, in fact, could compete against the current vessels?

Mr. **Scocozza**. I think it would be—because there are vessels of Panamax size in the market already, they would have a better opportunity to compete because their costs would be lower. The debt service on the Panamax vessels after they paid back would be so much higher. They couldn't even compete with their own class.

I certainly don't want to make any judgments for the market, Mr. Chairman. Maybe the Panamax vessels have different statistics or different information, so I certainly would not want to put a dark curtain around them. I think this would probably be a more appropriate line of questioning for them specifically, to speak about how they might be able to compete if they did pay back.

The information we have in our analysis would suggest their debt service would be much higher; their costs would be higher for providing the same service as their competitors.

Mr. **Biaggi**. Mr. Secretary, soon the DOT supplemental appropriation will reach the House floor with a prohibition on this rulemaking. While I am contemplating an amendment to delete that prohibition, I am concerned that the rule would then go forward without an opportunity to fully explore the various compromises now being discussed.

Is there any possibility to temporarily delay that rule for several months while good faith negotiations continue?

Mr. SCOCOZZA. At this particular time, Mr. Chairman, I don't see the opportunity for—what we did in the rule was to try to take into consideration all of the different views and put together what we felt was the best for all involved. We felt that the 1-year window was the best summation we could clearly do.

I would suggest, Mr. Chairman, that as this committee, this good committee, is involved in negotiations with the private sector, understand that our rule does not mandate any payback. The carriers don't have to pay back. If they are working with this committee—we are just providing a tool that the private sector can use. If they choose not to and choose to pursue a legislative remedy, they are free to do so.

Nothing will automatically happen on June 6 unless the individual carriers, which you might be working with, want something to happen otherwise.

Mr. BIAGGI. Except if you have the rule in place, it is a disincentive to negotiate in good faith. That is the only difference. We have been trying to compromise this situation. We realize what the issue is, and then with the implementation of the rule, that possibility seems to evaporate. That is our concern.

Mr. SCOCOZZA. I appreciate that, Mr. Chairman.

Mr. BIAGGI. Thank you, Mr. Secretary.

It has been suggested that funds from an ODS buyout could be used for CDS repayment. Is that possible?

Mr. SCOCOZZA. No; that is not the case, Mr. Chairman. They cannot.

Mr. BIAGGI. That seems to be the concern of some of the operators.

Thank you very much, Mr. Secretary. Nice to see you again. I apologize for not being here earlier.

Mr. SCOCOZZA. I am delighted to be here, Mr. Chairman. Thank you and the members of the committee for having us.

Mr. BIAGGI. I appreciate your being here. You are always cooperative, and informative, and unyielding. [Laughter.]

The next panel will represent those supporting CDS repayment. I recognize the gentleman from California, a most esteemed member of this committee, Mr. Anderson.

Mr. ANDERSON. Thank you, Mr. Chairman.

I asked the privilege of introducing one of the witnesses who comes from my district. It is with great pleasure that I welcome Stephen Oettinger, the vice president of Arco Marine, Inc., of Long Beach, CA, to these subcommittee hearings.

Arco Marine is a subsidiary of the Atlantic Richfield Co. It is responsible for the movement of Arco's Alaskan North Slope crude by tanker from Valdez to various west coast ports, including the Port of Long Beach.

Arco Marine is the owner of eight nonsubsidized Jones Act vessels ranging in size from 70,000 deadweight tons to 189,000 deadweight tons. In addition, it is the operator of two construction-differential subsidy vessels of 262,000 deadweight tons owned by the Atlantic Richfield Co.

In 1984, Arco Marine moved 161 million barrels of crude oil.

Mr. Oettinger is here to testify in favor of the Department of Transportation's rulemaking on the CDS payback. Although he has expressed some reservations about the two bills before the subcommittee, he is willing to work with us to reach a compromise.

I just wanted to welcome Stephen Oettinger here this morning. We are very happy to have you.

Mr. BIAGGI. Joining Mr. Oettinger is Capt. Gareth J. Thomas, president of Moore McCormack Bulk Transport; Thomas J. Mills, Esq., from Kominers, Fort, Schlefer & Boyer, representing Philip J. Shapiro, vice president and general counsel for Apex Marine Corp.; Roy G. Bowman, Esq., Bowman, Conner, Touhey & Petrillo, representing American Petrofina; Eugene Rose, president and chief operating officer of Seatrain Lines, Inc.; accompanied by Alvin Green, vice president, secretary, and general counsel of Seatrain Lines; and Donald R. Brinkley, vice president, transportation, Sohio Oil Co.

Before you go further, I would like to note that this is the third hearing on construction-differential subsidy repayment we have had in as many years. Proponents and opponents of repayment have had a full opportunity to make their views known and the subcommittee is fully aware of the arguments. There are merits on both sides.

We would like to concentrate on the compromise bills before this subcommittee or any other compromise which fairly addresses the needs of all parties. Let me emphasize—we know the arguments. If you are here to repeat the arguments, you are wasting your time and you are wasting ours. We know them. We would like your comments on the legislation.

Mr. Oettinger.

[Statement of Mr. Oettinger follows:]

STATEMENT OF STEPHEN R. OETTINGER, VICE PRESIDENT, ARCO MARINE INC.

I appreciate your invitation to express our views on payback of Construction-Differential Subsidy ("CDS").

Arco Marine, Inc. is the operator of the tank vessels *Arco Independence* and *Arco Spirit*, which are owned by Arco Marine's parent, Atlantic Richfield Company ("Arco").

The *Arco Independence* and *Arco Spirit* are very large crude carriers ("VLCCs") each of 262,000 dead-weight tons ("DWT") built with CDS in 1976 and 1977. In addition, Arco Marine is the owner of eight nonsubsidized Jones Act tankers ranging from 70,000 DWT to 189,000 DWT all of which are engaged in the transportation of Alaskan North Slope crude oil from Valdez, Alaska, to the United States west coast.

Under the Merchant Marine Act of 1936 and rules promulgated by the Federal Maritime Administration, CDS vessels over 100,000 DWT may transport crude oil from Valdez to Panama upon receipt of permission to do so. From Panama the crude oil is shipped via pipeline and tankers to the U.S. Gulf Coast. Any owner of an unsubsidized Jones Act tanker over 100,000 DWT may file a protest opposing the application. The Maritime Administration may grant permission to enter the Valdez-Panama trade for a maximum of six months in any twelve month period, only if the Maritime Administration determines that nonsubsidized vessels over 100,000 DWT will not be displaced. Applications are denied when unsubsidized vessels over 100,000 DWT could meet the need to be filled by the CDS vessel.

A total of nine CDS VLCCs were built in the 1970's in the expectation that they would be utilized in the foreign trade. Because of the significant changes in the world crude oil market, there has been no viable economic foreign trade for these vessels. In recent years, Arco has sporadically chartered its VLCCs for Strategic Petroleum Reserve cargoes but the future of this program is uncertain.

After the start-up of production of crude oil from the Alaskan North Slope, there was a need to utilize the CDS vessels over 100,000 DWT to transport Alaskan oil to Panama for transshipment to the U.S. gulf coast.

Subsequently, because of a variety of factors, including an increase in west coast crude oil demand and new vessels entering the trade, the Maritime Administration significantly decreased the number of applications it has granted to permit CDS vessels to enter the domestic market. In fact, neither of Arco's CDS vessels has been permitted in the domestic trade since January, 1984.

When Arco cannot economically operate its vessels in either the foreign or domestic trades, it is forced to lay them up at a cost of approximately $4,300,000 per year per vessel. Without a viable prospect for employment in the future, the Company would be forced to consider scrapping the vessels. We believe other CDS vessel owners face the same reality.

This would prove an economic tragedy not only for the vessel owners but also for the nation. The CDS vessels which have been employed in the Alaska-Panama service are generally newer, are significantly larger and are more economic than most of the other vessels serving this trade.

Recognizing these facts, the Department of Transportation ("DOT") on January 31, 1983, published a proposed rule for comment which would permit owners of CDS vessels to repay their subsidy with interest and thereupon enter the domestic trade. More than 150 comments were received on the proposed rule.

In the last two congressional sessions, riders attached to the Appropriations Acts denied funds first until June 15, 1984, and then until May 15, 1985, for the enforcement of any rule respecting CDS payback.

On May 3, 1985, the DOT issued its final regulations on CDS payback. These new regulations are similar to the original DOT proposed rule and simply permit the owner of any vessel built with CDS to repay the unamortized subsidy with interest by June 6, 1986. Upon subsidy repayment, the domestic trading restrictions will be permanently rescinded.

We support the new DOT regulations. The regulations clearly promote competition and we believe will result in lower transportation costs for the movement of Alaskan crude oil.

There will also be a substantial budgetary impact of CDS payback. While we do not at this time have board approval to repay the subidy, the government would receive approximately $80,000,000 if the subsidy was repaid on both Arco vessels. With high deficits threatening the nation, a program which could result in the return of hundreds of millions of dollars to the government is attractive.

We are aware that there are a number of proposals for legislative action affecting CDS payback. These proposals are apparently aimed at granting some relief to owners of principally smaller, older vessels who fear that they will not be able to compete once the domestic trading restrictions on CDS vessels are rescinded.

We believe that in our economic system those who provide the most efficient services should survive and those who do not must either become more efficient or retire from the business. Nonetheless, we have always been willing to discuss reasonable measures designed to accommodate divergent interests. With this in mind, I wish to discuss two recent bills.

Chairman Walter Jones has circulated a bill which, as of the date of this writing, has not been formally introduced. The Jones bill would provisionally permit any CDS vessel to enter the domestic trade upon receiving permission from the Secretary and upon the repayment of the subsidy with interest. The provisional permission could be revoked, however, if any unsubsidized vessel owner files a notice of harm stating that he cannot compete in the coastwise trade because of the operation of the CDS vessel.

While this proposal purports to be a compromise between a total prohibition on CDS payback and full payback, in fact, it is not a compromise. If the favored position of those who cannot compete must be preserved, there is substantial doubt that any CDS vessel would payback the subsidy and enter the trade.

The Jones bill is more restrictive than § 506 of Merchant Marine Act of 1936 as presently enacted and the Maritime Administration Regulations thereunder. As I noted above, under existing regulations only unsubsidized vessels over 100,000 DWT can protest any application for temporary employment of a CDS vessel in the Valdez-Panama trade. Under the Jones bill any unsubsidized vessel over or under 100,000 DWT could, in effect, block the entrance of the CDS vessel into the trade. Thus this bill represents a substantial step backward and will saddle this nation with obsolete and costly transportation.

H.R. 2485 has been introduced by Subcommittee Chairman Mario Biaggi. It would grant any CDS vessel the right to enter the domestic trade for periods totaling one-half of the remaining 20-year economic life of the vessel since construction upon the repayment of one-half of the unamortized subsidy with interest. The CDS vessel could operate for periods of one or two years at a time. The bill vests in the Secretary of Transportation the power to designate the years during which the vessel could operate in the domestic trade to promote competition or avoid overcapacity.

The Secretary should not be vested with this authority because we believe that the market place should allocate resources. It will be more difficult to establish the commercial relationships necessary to efficiently operate or employ a CDS vessel, if the government determines when the vessel will operate.

We also believe that the imposition of interest upon the subsidy repayment coupled with a restriction on length of service is inappropriate. As noted above, there appears to be no viable international trade for the CDS vessels. When they are not operating in the domestic trade, they will most likely be laid up at considerable cost. Under Section 506 of the Act and the existing regulations, no interest is imposed when a CDS vessel is permitted temporary employment in the domestic trade. The imposition of interest as set forth in H.R. 2485 would constitute a penalty and is, therefore, unacceptable.

While we have the significant reservations about H.R. 2485 as stated above, we believe it could provide an acceptable vehicle from which to fashion a compromise which we may support. Although we favor unrestricted domestic trading privileges upon full payback of subsidy with interest, restricted entrance of CDS vessels into the domestic trade for periods not exceeding half of their remaining economic lives is acceptable if the bill designates specific periods of at least one year when the vessels will have the absolute right to enter the trade upon repayment of a pro rata portion of the subsidy. The pro rata repayment of CDS must also be without an interest penalty. Such a bill would insure that the government will receive significant revenues through pro rata subsidy payback while protecting the unsubsidized fleet from competition of half of the CDS fleet.

STATEMENT OF STEPHEN R. OETTINGER, VICE PRESIDENT, ARCO MARINE INC., LONG BEACH, CA

Mr. OETTINGER. Thank you very much, Mr. Chairman.

I would like to take this opportunity to thank Congressman Anderson for that introduction. We look forward to continuing to work with him on critical issues in the district.

I appreciate the opportunity to represent the views of the Atlantic Richfield Co. on CDS payback and, honoring your request, will basically look at the bills that have been proposed as a potential vehicle for compromise.

Before doing that, I would just like to briefly talk about the rule and our reason for supporting it as it directly impacts Arco Marine.

We believe that there is a need for some restructuring in the marine industry, and we want the opportunity to use our CDS vessels because they provide lower cost transportation to us. That phenomenon is consistent with all the major industries in this country as we try to be as competitive as possible.

Over the last 18 months, if you take a look at our two CDS vessels, they have not had much economic employment. The strategic petroleum reserve business, we have had a few trips on that. That is, unfortunately, being indefinitely postponed by September of this year, and the last time we have operated on a waiver was January 1984. When the vessels are in layup, they each cost us about $4.3 million a year.

I won't repeat the basic arguments, the other arguments, supporting the rule. I would also like to say that we are opposed to the position of AIMS, the American Institute of Merchant Shipping. They will be testifying in the next panel. They are in opposition to the Department of Transportation rule.

The other preliminary comment that I would like to make is that we believe that your committee, Mr. Chairman, should be the one that is formulating the maritime policy for this country. We were very concerned when the supplemental appropriations amendment was passed and the potential impact that it would have on the repayment issue.

As I mentioned, we are very supportive of the free market working and striving for the economic benefits for the most efficient operators. However, we do recognize that there are different opinions on this issue, and we would be willing to work toward a compromise.

We have looked at the legislation that you have offered and we think it might have potential for a compromise vehicle if two changes were made. The two changes would, one, involve the discretion of the Secretary of the Department of Transportation. It is very difficult from our standpoint, when we have to move roughly 400,000 barrels a day of the Alaskan North Slope crude, to be faced with the uncertainty of when we could operate in either the 2- or 4-year time period that is contained in your legislation. We need that provision removed. We need to have certainty there.

The other aspect of your bill, Mr. Chairman, is that we don't think it is appropriate to have to pay interest on the repayment piece. When we have operated in waiver service over the last several years prior to January 1984, according to the laws and the regulations, we are not required to make a repayment of interest. When one is operating only 50 percent of the time and that is the likely situation because there will be no foreign employment, we think that is an excessive penalty to place on the operator.

If those two changes were made, we think that might be the kind of vehicle or structure that we might be able to support as a compromise in trying to solve this very difficult issue.

We would also like to commend you, Mr. Chairman, for making a continuing effort to resolve these issues. You have been willing to step out in front, and we want to be very supportive of that.

Regarding Chairman Jones' bill, we have noticed today that there was a change in it where one had 3 months to repay the subsidy, but when one is talking about tens of millions of dollars, and in the case of Atlantic Richfield, if we repaid the subsidy on both vessels—and I would like to say we have not, as of this point in time, had board approval to do it—we would be looking at something in excess of $80 million. One does not run into those kinds of decisions quickly. It must be apprised——

Mr. **Jones**. Would the gentleman yield at that point? Would you yield to clarify a point?

Mr. **Oettinger**. Yes.

Mr. **Jones**. I think the language in the bill which we have introduced does not require repayment but merely to make the application in the 3 months, and you would have the entire year in which to make the payment.

Mr. **Oettinger**. I have not seen the language, Mr. Chairman, so it is difficult for me to comment on that specific aspect.

Based on the language that we have seen prior to today, the general form of your bill would be difficult for us to compromise on.

Those are the comments that I would like to make at this point in time. I would be more than happy to answer specific questions later on.

Thank you.

Mr. Biaggi. Captain Thomas.

[Statement of Captain Thomas follows:]

Statement of Gareth Thomas, President, Moore McCormack Bulk Transport, Inc.

Mr. Chairman, I am Gareth Thomas, President of Moore McCormack Bulk Transport, Inc., which operates three 38,000 dwt tankers constructed with the aid of construction-differential subsidy in the mid-1970s for operation in the foreign trades. They are operated under Operating-Differential Subsidy Agreements entered into with the Maritime Administration. At the time of their delivery, they had intermediate term charters from a major oil company which have now expired. In the present climate it is difficult to obtain profitable employment for the vessels in the foreign trades. The vessels have, however, been employed sporadically in the preference trades. Since the outlook for profitable employment for the vessels in the foreign trades is so bleak, Moore McCormack Bulk may decide to repay its CDS in accordance with the rule promulgated by Secretary Dole. Therefore, Moore McCormack Bulk strongly supports the Secretary's action in adopting the final rule permitting CDS repayment.

We believe the Secretary was correct in determining that the subsidy program for tankers has failed. Furthermore, we believe the Secretary was correct in agreeing to recoup for the government as much of the wasted subsidy dollars as is possible. The rule would permit Moore McCormack Bulk to repay its CDS with interest and release the government from its future ODS obligations in return for the right to enter the domestic trades on a permanent basis. If Moore McCormack does repay its CDS with interest and terminates its ODS contract, the government may recoup CDS and save ODS in an amount of more than $100 million. Let me stress for the Committee that this $100 million reduction in the budget deficit will be in addition to the nearly $600 million which will be recovered or saved by virtue of the repayment of CDS and the cancellation of ODS contracts by the owners of the VLCCs and the Panamax-sized vessels. At a time when concern about budget deficits is preoccupying the minds of both Congress and the public, we believe that the correct course of action is to permit the rule to become effective.

Mr. Chairman, Moore McCormack Bulk has examined both H.R. 2485 and H.R. 2550. We believe that both bills represent a sincere effort by their respective authors to find a compromise solution to the controversy over CDS repayment. However, I regret to say that Moore McCormack Bulk cannot support either of these bills in their present form. It should be noted that both bills add a new requirement for the repayment of interest by vessels which are allowed to participate in the domestic trades only 50% of the time. Such a requirement will make the cost of these vessels so high that they will be unable to obtain employment in the domestic trade. Similarly, we believe that both bills are much too solicitous in their effort to protect less efficient domestic trade vessels from competition.

Let me conclude, however, on a positive note, Moore McCormack Bulk is willing to discuss with all interested parties a solution to the controversy which will enhance the efficiency of our merchant marine. We believe it is time that both subsidized and unsubsidized operators of vessels look beyond their parochial interests and work together to resolve this controversy in a fair manner which protects the interests of all the parties.

STATEMENT OF GARETH J. THOMAS, PRESIDENT, MOORE McCORMACK BULK TRANSPORT, STAMFORD, CT

Mr. Thomas. Mr. Chairman, after what we have heard this morning about the advantages for the larger tankers paying back CDS, let me say that I come from the smaller end of the operation with in Moore McCormack only three 38,000-ton tankers. Without going into the arguments for and against payment again, let me say that we do see CDS payback as something that could be attractive to the smaller vessels.

We are in the process of carrying out discussions with various charters in the trade, and are bullish on the prospects of being able to employ these ships in domestic trade profitably. Therefore, we clearly strongly support the rule as it stands.

However, let me say, to act on a more positive note, we are in Moore McCormack willing to discuss with all interested parties the possibility of some form of compromise as a solution to the controversy that exists, which will enhance the efficiency of our merchant marine.

We believe it is time that the subsidized and unsubsidized operators look beyond their parochial interests and work together to resolve this controversy in a fair manner to the interest of all parties.

Thank you.

Mr. BIAGGI. Mr. Mills.

[Statement of Apex Marine Corp. follows:]

STATEMENT OF PHILIP J. SHAPIRO, VICE PRESIDENT, APEX MARINE CORP.

Mr. Chairman, I am Philip J. Shapiro, Vice President and General Counsel of Apex Marine Corp., the managing agent for subsidized vessels operated by Aeron Marine Shipping Company, American Shipping, Inc., Aquarius Marine Company, Aries Marine Shipping Company, and Atlas Marine Company. All of these companies own and operate 90,000 dwt tankers except Aries Marine Shipping Company which operates two OBOs of 80,000 dwt. All of these vessels were constructed with the aid of construction-differential subsidy. Captain Leo V. Berger is the principal owner of these companies and they are collectively known as the "Berger Group." I am accompanied here today by counsel, Thomas L. Mills, of Kominers, Fort, Schlefer & Boyer.

I wish to compliment and thank the Chairman for the hard work and sincere efforts which have resulted in both H.R. 2485 and H.R. 2550. Both bills are an attempt to find a compromise solution in the controversy over CDS repayment. The Berger Group has consistently expressed its willingness to sit down with all other parties to the controversy and join in an attempt to find a solution which would be a reasonable compromise. I regret to say, however, that I am here to testify in opposition to both bills in their present form.

Before addressing the deficiencies in the bills however, I would like to discuss briefly the final rule permitting CDS repayment which was promulgated by Secretary Elizabeth Dole on May 3, 1985. Mr. Chairman, the Berger Group believes that the Secretary's action is the most significant deregulatory maritime action adopted by the Reagan Administration to date. Secretary Dole estimated that the federal government will receive as much as $378 million of repaid CDS and interest, if all of the owners of VLCCs and Panamax class tankers elect to repay their CDS. She also estimated that the federal government could save as much as $18.3 million per year in unexpended operating-differential subsidy if the Panamax tankers elect to repay their CDS and terminate their ODS contracts. The ODS savings, on the Panamax tankers alone, will total nearly $200 million over the next 10 years. Thus, the government will recover or save nearly $600 million of subsidy which was previously thought to have been wasted. The Berger Group believes that an action recouping moneys thought to have been wasted is without precedent and the Secretary should be commended for her significant contribution to the reduction of the federal deficit.

Moreover, as the Secretary stated in her landmark decision, the rule will also result in lower transportation costs, open competition and greater transportation efficiency. The Secretary estimated that the transportation savings will be in the range of $800 million to $3.3 billion depending upon the economic conditions prevailing in the trade. Thus, the adoption of the rule benefits the shippers and consumers of Alaskan oil as well as the nation's taxpayers.

The Secretary noted that the only negative consequence which may result from adopting the rule is a reduction in "the employment opportunities of the smallest, oldest and least efficient tankers in the ANS trades, although at least initially there may be employment problems for some larger tankers currently active in the ANS trades." In a worst case scenario, the Secretary determined that 13 tankers under 55,000 dwt and three tankers over 55,000 dwt would be unemployed as a result of repayment of CDS. Nearly all of these vessels will be over twenty years old. Therefore, the Secretary concluded "the overall effect of CDS repayment will be a stronger, more viable U.S. merchant marine."

Mr. Chairman, the Berger Group believes that the best policy option for this Committee is to allow the newly promulgated rule to become effective and to let the marketplace determine which vessels will elect to repay their subsidies. It is a truism, that free and unfettered competition is a long-standing American tradition. Moreover, at this time of great public concern over the size of the federal deficit, the budgetary impact of the recoupment of nearly $400 milion of CDS is very significant. Indeed, the budget resolution adopted recently by the Senate contemplates that the sum of $200 million in CDS will be repaid during fiscal year 1986. If this Committee takes action to prevent CDS repayment, then other valuable government programs will have to be reduced by greater amounts in order to reach the level of deficit reduction that both Houses of Congress have targeted. In our view such a result would be tragic.

The owners of the present Jones Act tanker fleet contend that it would be unfair to permit the subsidy-built and operated tankers to invade their trade. The notion that the present Jones Act fleet is unsubsidized is a fabrication. They are subsidized by the high rates in both the Jones Act trade and cargo preference trade. Indeed, in the past those rates have been so high that their subsidy is greater than ours. The irony is that in order to obtain less subsidy, Captain Berger was legally required to dispose of nearly twenty foreign-flag vessels while several other large Jones Act tanker operators used their exorbitant profits from the Jones Act to greatly expand their foreign-flag fleets.

The Jones Act protects domestic operations from foreign competition in order to promote a strong and modern American merchant marine. The cost of doing so—the subsidy—is borne by the U.S. consumers who pay the higher resulting freight rates. The siphoning of profits earned in the Jones Act trade to build and support foreign-flag vessels is a flagrant violation of that policy. If a subsidized operator were to use his direct subsidy for that end he would violate the law.

Although the rates for tankers in the Jones Act trades are currently lower than in the past, if the subsidized tankers are not permitted to participate in that trade these rates will soon climb, once again, to exorbitant levels. In the long run, exorbitant rates hurt the merchant marine. Alternative methods of transportation are developed. The Colonial Pipeline which has displaced our East Coast product tanker fleet and the pipeline across Panama are examples of this phenomenon. Do the opponents of payback believe that our merchant marine will be better off if it becomes necessary to transport Alaskan oil by pipeline from the Pacific Coast to the Gulf Coast refineries instead of permitting the subsidized tankers to repay subsidy and enter the trade? This committee is aware of the current attempts to destroy our cargo preference laws and to permit the export of Alaskan crude oil. Those efforts will only be intensified if exorbitant rates are permitted to continue in the Jones Act and cargo preference trades. The Berger Group believes that only an efficient merchant marine operating at reasonable rates is entitled to the protection against foreign-flag vessels afforded by both the Jones Act and the cargo preference statutes.

It should also be noted that the absence of the efficient low cost CDS-built VLCCs for the Valdez-Panama movement during 1984 reduced the flow of Alaskan crude oil to the Gulf and East Coast. This is so because the higher rates demanded by smaller vessels made it uneconomical to move the oil long distances. Thus, producers were forced to "shut in" local California crude production to the detriment of the consumer.

As I stated at the beginning of my testimony, the Berger Group has consistently expressed its willingness to consider all proposals for a legislative compromise solution. However, I must state that in our view, both of the pending bills constitute a step back and a not a step forward from the situation which prevails under Section 506 at the present time.

Under Section 506, the Secretary may grant a waiver for a subsidized vessel to enter the domestic trade for six months in any year whenever she determines "that such transfer is necessary and appropriate to carry out the purposes" of the Act. The owner must repay a proportionate share of the CDS, however, the repayment is without interest. In June 1977, the Maritime Administration prescribed regulations governing waivers for the participation by vessels over 100,000 dwt built with the aid of CDS in the carriage of Alaskan oil in the Valdez-Panama trade. This program, however, has proven to be totally inadequate. Under the Maritime Administration's regulation, no six-month waiver can be granted unless every single vessel in the fleet of more than 100,000 dwt is already chartered. Thus, for example, in

January 1984, the Maritime Administration forced the removal of 750,000 dwt of subsidized tankers from the Alaskan trade to compel the shippers into hiring smaller vessels on short-term charters at exorbitant rates. Moreover, the regulation makes no provision for the use of Panamax size vessels (below 100,000 dwt) in the Alaskan trade and waivers for that size vessel to participate in that trade have been an extremely rare phenomenon in the last eight years.

Mr. Chairman, enactment of either of the bills pending before the Committee would only add to the deficiencies of the present waiver regulations.

Firstly, both bills require that the repayment of the proportionate share of CDS contain interest on the subsidy. While it may be appropriate to require the repayment of interest when CDS is repaid in its entirety, thereby permitting the permanent deployment of the vessel in the domestic fleet, the Berger Group believes that it is unfair to impose that requirement on vessels which will participate in the Alaskan trade only 50% of the time. The Secretary noted in her decision that the requirement to repay CDS with interest will result in the vessels which repay their subsidy having a substantially higher capital cost than their competition; a fact which the Berger Group has constantly reiterated to this Committee. It may be fair to impose that requirement on subsidized vessels which are permitted to operate full-time in the domestic trade. It is unfair, however, to impose that onerous requirement on subsidized vessels who will only be permitted to alternate between periods of employment in the domestic trade and lay-up. Such vessels must earn during their tenure in the domestic trade enough revenue to pay their basic capital costs for twice the period of their employment plus an amount to cover the proportionate repayment of CDS. Moreover, such vessel owners bear the additional costs of preparing their vessels for and removing their vessels from lay-up. A requirement that such vessels also pay interest on the CDS could raise the rates to a level where they could not find employment.

Secondly, both bills contain standards which limit the Secretary's authority to admit vessels into the domestic trade which are harsher than those administered under the present regulations. The Jones bill permits any owner of an unsubsidized vessel to file a notice of harm; the current regulations only permit owners of vessels of greater than 100,000 dwt to protest applications by VLCCs to enter the domestic trade. The bill also requires the Secretary to expel the subsidized vessel from the trade if he determines on the basis of the notice of harm that the unsubsidized vessel cannot compete in the coastwise trade. Thus, under this bill, the owner of a 50,000 dwt product carrier could compel the expulsion of a 265,000 dwt tanker from the Valdez-Panama trade and a 35,000 dwt product carrier could compel the expulsion of 90,000 dwt Panamax size tanker from the Panama-Gulf Coast movement despite the fact that the employment of the vessels will require the shippers to pay exorbitant rates for inefficient vessels in those trades. Accordingly, the approach contained in that bill is not one which the Berger Group can support.

Similarly, under H.R. 2485, the Secretary is authorized to designate the years during which a subsidized vessel may operate in the domestic trade solely on the basis of competitive effect and overcapacity without regard to the shipper's additional costs for the use of small inefficient vessels. We believe that both of these bills contain standards which are overprotective of the domestic fleet without giving adequate consideration to the interests of the owners of subsidized vessels and the shippers and consumers of Alaskan crude oil.

Mr. Chairman, let me conclude, by once again reiterating the Berger Group's willingness to sit down with all of the interested parties in order to fashion a compromise solution. Such a solution must be, however, one which will enhance the efficiency of our merchant marine and provide the necessary financial benefits to the shippers and consumers of Alaskan oil.

STATEMENT OF THOMAS L. MILLS, ESQ., KOMINERS, FORT, SCHLEFER & BOYER, WASHINGTON, DC, REPRESENTING APEX MARINE CORP.

Mr. MILLS. Mr. Chairman, thank you.

Let me first, if I may, respond to a question perhaps that you have raised with Mr. Scocozza about the Panamax-sized vessels since the Berger Group, of course, operates Panamax-sized vessels.

We testified before you, Mr. Chairman, and this committee twice to precisely the same economic facts that you referred to, and that is that when we pay back CDS, we are more expensive than the exact ships in the trade. The question then—that fact led the Department of Transportation to conclude that it would, therefore, would be unlikely that the Berger Group would repay on these Panamax-sized vessels.

What they failed to take into account, however, are the economic factors which have prevailed in the trade, and that is the extraordinarily high profit margins which have inhered in that trade, such that if we pay back, there is a likelihood that we could pay back and still make a little money. What that would mean, of course, is that the guys with the vessels just like ours would still make money and of course still make more money. Therefore, we would not have a devastating impact on them.

We are, of course, highly more efficient than any of the ships under 50,000 tons. That efficiency, of course, would be passed on to the consumer, the taxpayers of the United States.

Again, we emphasize that the rule permits payback. It does not mandate it. Whether we would pay back and how many of our ships we will pay back will be a market decision, if the Department of Transportation's rule continues in effect. We think that is as it should be, that that is where the decision ought to be made.

Now if I could, Mr. Chairman, let me turn to your bills, your bill and Chairman Jones' bill. I regret that we did not have a copy of the printed bill of Chairman Jones until after we had prepared our testimony and analyzed it, and the effective date, which is September 1, 1985, which is the last paragraph of the printed bill, was not in the earlier draft that we saw. So the 3-month window aspect escaped us altogether.

We view that as a highly positive sign. We commend Chairman Jones on that aspect of the rule. It leads us to a completely different analysis of the chairman's bill.

If it is his intention to create a window of full payback under the rule with thereafter a continuing process whereby the trade might be supplemented with additional vessels, then I think that that is an excellent basis upon which to begin to look at a compromise, understanding that we are not committing to anything.

I compliment the chairman and his counsel and staff for looking for a positive vehicle.

At the same time I have to mention and bring to this committee's attention that, if we are talking about a 3-month window which is in the bill now, September 1, 1985, we are staring at hearings here; we are looking at court litigation; we are looking at, of course, the rather devastating impact of the potential appropriations bill stopper.

We, of course, were dismayed and very unhappy about that. We think the maritime policy ought to be made here by the committee with substantive jurisdiction who knows the arguments. We doubt very seriously that the members of the Appropriations Committee were sufficiently informed upon these delicate issues to make a reasoned judgment.

That leads us to the point that you raised just previously, Mr. Chairman. That is you were concerned that the effectiveness of the rule would somehow provide a disincentive to we, the proponents of the payback, from wishing to consider a compromise. I think that history has shown just the opposite is true. I think, Mr. Chairman, that we have been very clear all along that we, of course, are willing to listen to you to follow your great leadership and to deal with you to try to work out something which may not be the whole ball of wax for us but would not be the whole ball of wax for the other side.

We are open to compromise. We are open to discussion. We have been; we remain it. I think that record is clear.

On the other hand, Mr. Chairman, it is our side of the issue which has faced the brunt of the constant statutory delays in the process. Now we have not had the opportunity to pay back through, lo, these many years that we have had this problem. Yet, the other side of the issue has shown no indication, no willingness, whatever, to consider any compromise whatever.

Mr. Chairman, I think that you might be preaching to the choir if you are talking to us about compromise. I hope that you will have some very nice words for the witnesses who follow, sir.

Mr. Biaggi. Yes. I thank you.

Clearly, that is what I am doing, but the object of my comments were valid. They obviously did not apply to you. We know that you have been prepared to compromise.

We will have a 10-minute recess in order to respond to the vote on the floor.

Mr. Mills. Thank you, Mr. Chairman.

[Recess taken.]

Mr. Biaggi. The meeting is called to order.

Mr. Mills.

Mr. Mills. Mr. Chairman, if I could resume just briefly, I have about completed my statement.

I would like to address the title XI issue, to which both you and Chairman Jones address yourselves.

Chairman Jones indicated his desire that title XI be made available in accordance with the statute in order for vessels that would pay back to pay back, and that is something I think all of us at the table would support.

Now the chairman's bill, with the September 1, 1985 date, that would give us basically 3 months, as the chairman pointed out. You can hardly get a title XI application through in 3 months, so that is a problem.

Now on the point, Mr. Chairman, that you raised as to the dire position that the title XI program finds itself in, it is true that it is in tough shape and it is true that the fund, the reserve fund, the revolving fund used for paying defaults is nearly depleted, and, therefore, there will have to be borrowings against the Treasury.

Let me emphasize that if applications were granted to high quality projects, there is plenty of guarantee authority; that is, to issue new commitments. The higher quality, new applications which can be granted will increase the income to the fund and probably prolong that.

Those are the only two points that I wanted to make on that. I will defer to the next witness.

Mr. Biaggi. Mr. Bowman.

[Statement of American Petrofina, Inc., follows:]

STATEMENT OF AMERICAN PETROFINA, INC.

This statement is submitted to the Subcommittee by Roy G. Bowman, Esq., of Washington, D.C., on behalf of American Petrofina, Incorporated, on the issue of repayment of construction-differential subsidies ("CDS") by owners of U.S. flag merchant vessels. We appreciate the opportunity to express these views to the Subcommittee.

American Petrofina, Incorporated, often referred to by its trade name, "Fina", is a Delaware corporation with its principal place of business in Dallas, Texas. Fina has, since 1956, been engaged in the exploration for oil and the transportation, refining, and marketing of crude oil and refined petroleum products throughout the United States. In addition, Fina manufactures and markets petrochemicals and plastics. Fina employs over 3,500 people in 27 states, and its stock is traded on the American Stock Exchange.

The major portion of Fina's business is the refining of petroleum products. Fina has only limited sources of its own crude oil and as a result is largely dependent upon other companies for supplies of feedstock for its refineries. In 1972 and 1973, Fina, interested in developing a reliable source of transportation for the foreign crude oil which then made up most of its purchased, entered into 25-year time charters for two 225,000 deadweight ton tankers which were built in the U.S. with the aid of CDS. These ships, the *Brooklyn* and the *Williamsburgh*, were delivered in 1973 and 1974, respectively. Since they were built in part with CDS, they are generally restricted to employment in the foreign trade under the Merchant Marine Act, 1936.

Almost simultaneously with the delivery of the *Brooklyn* and the *Williamsburgh*, the Arab oil embargo drastically and permanently changed the nature of the worldwide crude oil trade and the economic realities of tanker operations. The precipitous drop in the demand for foreign oil, both in the U.S. and abroad, the unprecedented rise in fuel costs, and the oversupply of large tankers made it uneconomic to employ very large crude carriers ("VLCCs") like the *Brooklyn* and the *Williamsburgh* in the foreign trade. From 1975 to 1979 these vessels operated in the foreign trade only intermittently or were laid up overseas. Fina then brought the *Brooklyn* and the *Williamsburgh* back to the U.S., and neither vessel has had substantial foreign employment since then.

Without the possibility of economic employment in the foreign trade, the only realistic use for Fina's ships is in the domestic, Jones Act, trade, and specifically in the transportation of crude oil from Alaska to Panama.

Since 1980, Fina has engaged in a start-and-stop process of partial repayment of CDS for service in the Alaska oil trade pursuant to temporary waivers under Section 506 of the Merchant Marine Act, 1936. However, this arrangement, involving partial repayment of CDS without interest and entry into the Alaska trade for not more than 6 months in any twelve, is unfair to everyone. Neither the owners of existing Jones Act ships nor the owners of CDS vessels have any way of knowing if, or when, CDS vessels will be permitted to enter the domestic trade. Moreover, shippers seeking to arrange transportation must contend with the same uncertainty.

For Fina, the inability to arrange long-term charters for its vessels, the unpredictability of temporary waivers and the need to absorb all layup costs with only six months or less of employment, makes operations under the existing system of waivers both inefficient and costly. Other inequities under this procedure are created by the role of the Maritime Administration as a charter broker for the Alaska trades and by the repayment of CDS without an appropriate amount of construction period interest to achieve economic parity with unsubsidized vessels. The result is confusion and uncertainty for all participants and instability in the maritime industry.

To improve on what is clearly an unsatisfactory situation, Fina has had pending, since 1980, an application pending for total repayment of CDS with interest, in accordance with the statute as interpreted by the Supreme Court. Fina has consistently and regularly advocated full CDS repayment in formal proceedings in all three branches of the government since that time.

With the publication in the "Federal Register," on May 7 of amendments to 46 CFR 276.3, the Secretary of Transportation has brought about the most important development in the debate over the issue of CDS repayment since the Supreme Court's decision in 1980. The discussion accompanying the amendments to the regulations and the Regulatory Impact Analysis released on May 1 are of a uniformly high quality and are a credit both to the Secretary of Transportation and to her professional employees in the Office of the Secretary and in the Maritime Administration.

Fina believes that the rule produced by these efforts is an appropriate resolution of the conflicting interests that have surrounded the issue of CDS repayment for the last decade. No one should believe that the rule is one-sided in favor of the proponents of CDS repayment. The inclusion of a one-year limit on the period within which repayment can be made responds to one of the chief complaints of the opponents of payback, who have described CDS vessels as an overhanging threat to the market. The one-year restriction for repayment creates only a limited opportunity for CDS vessel owners who must commit enormous sums of money necessary to repay CDS based on a one year assessment of the market. As we have already seen, market conditions can change, sometimes very abruptly. With such a narrow window within which to make a repayment decision, the possibility of a CDS vessel "skimming the cream" is virtually non-existent. In addition, the interest provision of the rule penalizes the operator of a CDS vessel and actually makes his vessel more expensive than a comparable Jones Act vessel. Notwithstanding these deficiencies, Fina believes that the rule is a better solution to this difficult problem than any legislative proposals advanced so far.

If the Subcommittee nevertheless intends to pursue a legislative approach to these complex issues, Fina urges that any legislation this Subcommittee approves incorporate four principles.

First, all CDS repayment applicants should be treated equally. Until now this has not been the case. In recent years only two vessels have been allowed to make full CDS payback, and these vessels are both from the same company. This gives the appearance of favoritism, an appearance that is enhanced in view of the lack of action on Fina's application for CDS repayment which has been pending for almost five years.

Second, government intervention in the shipping markets should be minimized. No statute does and no policy should entitle the Jones Act fleet to protection from other U.S.-operated, U.S.-built vessels as long as entry costs are the same. Complete CDS repayment with appropriate interest places formerly subsidized vessels on an equal footing with unsubsidized vessels and is a wholly satisfactory mechanism to ensure fair competition. Upon repayment of CDS, with appropriate interest, there is no reason for the Maritime Administration to limit competition or act as a federal charter-broker of Alaska shipping. Such a system simply perpetuates commercial uncertainty, wasted investment, case-by-case regulation and litigation. This is a role to which government is not suited and which it has no business performing.

Third, there should be no further delay. The Supreme Court has held that complete CDS repayment has been the law since the inception of the CDS program. The Maritime Administration has allowed full CDS repayments from as early as 1964. MarAd has taken the position since 1977 that full CDS repayment on tankers would be of overall benefit to the U.S. merchant fleet. Fina has had an application for full CDS repayment on one of its vessels pending since 1980. Further delay will compound the waste of effort and resources that has already taken place and will extend unnecessarily the uncertainty facing the shippers, the operators of CDS-built vessels, the existing Jones Act fleet, and the shipbuilders.

Finally, any legislative resolution must deal with the treatment of those companies that have repaid CDS under the Department of Transportation's new rule prior to the effective date of any legislation. The legislative process takes time to complete. Yet, while deliberation of the legislative issues is proceeding, the one-year administrative limit on repayment will be eroding. Thus, it is likely that some companies will make repayment pursuant to the DOT rule before legislation can be enacted. If that occurs, it would be manifestly unfair to permit other companies to take advantage of an entry mechanism that requires substantially different capital costs. Therefore, any legislation must give those who have already repaid an opportunity to proceed under the legislation and to reverse their prior payment.

With respect to the two legislative proposals that have been advanced, we will direct our comments to their major features rather than to the details to their language. One draft bill would allow a CDS vessel into the domestic trade for a series of successive 6-month periods, under criteria similar to those in section 506 now. The eligibility of the vessel to remain in the domestic trade would be subject to challenge in administrative proceedings initiated by the owner of any non-CDS vessel. If the CDS-built vessel were allowed to remain in the domestic trade for 3 consecutive years, its owner would then be permitted, during a one-year period, to pay back all the remainding CDS, with interest, and to place the vessel permanently in the domestic trades. The interest would be repaid at Title XI rates even if the owner had financed the vessel at lower rates.

A notable feature of this proposal is that it provides a specific statutory basis for full CDS payback for all kinds of vessels, not just tankers. Fina is concerned, however, that operation in the domestic trade under six-month waivers in accordance with this draft would be even more restrictive than at present, making chartering much more difficult than it already is. Under present section 506, there is at least no statutory rule allowing an existing Jones Act operator to oust a CDS-built vessel before the end of the six months. Moreover, interest would be charged for entry for a six-month period, which is not the case under present practice. Since every existing Jones Act operator including those with vessels less than 100,000 dead-weight tons, could file a "notice of harm" once every 6 months, it is likely that notices of harm would be filed almost continually during the 3-year period before full CDS payback could be made. Moreover, MarAd's role in administering this program guarantees further governmental allocation of markets and the possibility of favoritism.

Chairman Biaggi's bill, H.R. 2485, would allow a CDS-built tanker into the domestic trades for 50% of its remaining economic life, upon repayment of half the unamortized CDS with interest. In effect, this would make half-time re-entry a matter of right, rather than a matter of discretion. However, this right could be secured only by the advance lump-sum payment of unamortized CDS plus interest, neither of which are currently required to be paid in advance. Within 60 days after the repayment, the Secretary of Transportation could designate which years will make up the 50% of the remaining economic life. Such a tanker could be in the Jones Act trade not more than one year out of each of the remaining successive 2-year periods in its economic life. The interest rates charged could be higher than those the vessel owner had obtained on its non-CDS financing.

This proposal, while avoiding many of Fina's objections to the other proposal discussed above, also includes administrative involvement in determining which years a vessel may operate domestically. It is unreasonable to expect that, given the difficulty of predicting future market requirements with any great degree of accuracy, the allocation of domestic trading slots could be on anything but an ad hoc basis. The result is the further unnecessary intrusion of the administrative process in the competitive marketplace that will make charter discussions impossible.

A further problem with H.R. 2485 is that it legislatively creates a class of ships limited to layup status. Certainly with respect to vessels in the VLCC class, such as Fina's, the long-standing evidence is that there are no economic foreign trading opportunities. In recent years, Fina's ships have been in layup whenever not temporarily employed in the domestic trade. While it is admittedly attractive to have broader domestic trading opportunities than are now available, any possibility of foreign employment is merely illusory during those years that domestic trading is not authorized. Consequently, the practical effect of the bill is to mandate layup for certain of the most modern and efficient vessels in the U.S. fleet. We believe that this is an inappropriate result.

To summarize Fina's views, while neither the final regulation nor the proposed legislation represent exactly the way in which Fina would have resolved this issue, we prefer the final regulation to the proposed amendments to section 506. Fina is always ready to discuss alternative approaches with opponents of repayment, but they have not indicated any interest in compromise. Moreover, the deficiencies in the bills discussed today demonstrate the difficulty in achieving a true compromise. We, therefore, urge that the Subcommittee do nothing to prevent the administrative process from going forward. After the many years it has taken for the Department of Transportation first to study and then to fashion a resolution of this problem, we fear that Congressional efforts to effect a different solution will take several more years. We believe that further delay would be harmful to all the parties to the debate.

STATEMENT OF ROY G. BOWMAN, ESQ., BOWMAN, CONNER, TOUHEY & PETRILLO, WASHINGTON, DC; REPRESENTING AMERICAN PETROFINA, INC.

Mr. **Bowman**. Good morning.

I am appearing here on behalf of American Petrofina this morning. I will just briefly summarize my testimony in light of the time.

American Petrofina is a Delaware corporation that time charters two of the CDS-built VLCC's, the vessels *Brooklyn* and *Williamsburgh*. Fina has been actively seeking to repay CDS on these vessels since 1980. In that year, Fina filed an application for repayment with the Maritime Administration. Notwithstanding the lapse of 5 years, no action has been taken on this application. Even though no action on Fina's application has been taken, two other VLCC's have been permitted to repay CDS.

In addition, the U.S. Supreme Court has ruled in that time that the CDS repayment is entirely appropriate as a mechanism for placing CDS-built ships in the domestic trade.

The rule that the Department of Transportation is promulgating is really a long-awaited resolution of the complex issues surrounding CDS repayment. Fina believes that the Department's analysis of the effect of the rule is, for the most part, careful and thoughtful. Accordingly, Fina fully supports the rule and believes it is a better solution to the difficult problems than the two legislative proposals we have seen so far.

Now, on the other hand, Fina has always been willing to compromise or settle on a different means of resolving these issues, but we don't see a satisfactory solution in the two bills that have been presented so far.

Both bills create substantial discretionary authority in the Maritime Administration. They insure continued uncertainty as to which vessels will actually enter the trade, and they create obstacles to efficient planning of the transportation requirements that Mr. Oettinger has already alluded to.

We believe that any legislation which addresses this issue should contain the following elements:

All CDS repayment applicants should be treated equally. MarAd should not have discretion to favor one operator to the disadvantage of another.

Second, Government intervention in the shipping market should be minimized. MarAd should not be vested with the role of Federal charter broker for the Alaska trade.

Third, there should really be no further delay in implementation of CDS repayment. The issue has been the subject of litigation and rulemaking proceedings for almost 10 years. The time has come for that to end.

Finally, any legislation must protect those companies which have taken advantage of the DOT rule and repaid CDS prior to the enactment of the legislation. The lapse of time involved in the legislative process, coupled with the 1-year limitation on repayment in the existing rule, creates the likelihood that some companies may repay before the legislation can be enacted. Therefore, the legislation, if enacted, must permit some mechanism for equalizing the applicants who have preceded and those who follow under a different scheme.

Finally, Fina is of the belief that these hearings will illustrate the complexity of reaching some adequate compromise and that, therefore, the best course of action is to permit the rule to go into effect. Nevertheless, we are willing to discuss any reasonable proposals.

Mr. BIAGGI. Mr. Brinkley.

[Statement of Mr. Brinkley follows:]

STATEMENT OF DONALD R. BRINKLEY, VICE PRESIDENT OF TRANSPORTATION FOR SOHIO OIL CO.

My name is Donald Brinkley and I am a Vice President of Sohio Oil Company, one of the business groups of the Standard Oil Company (Ohio). My area of responsibility encompasses Sohio's crude oil transportation activities, including its sizable marine operations. I appreciate the opportunity to appear before you today and present Sohio's view on the issue of payback of construction differential subsidies (CDS) by tanker vessels.

Since the opening of the Trans-Alaska Pipeline in 1977, Sohio has been and continues to be the largest shipper of Alaskan crude oil, transporting approximately 50% of the North Slope's 1.7 million barrel per day output. The company operates the largest chartered fleet of U.S. flag tankers in the industry, overseeing more than 30 vessels. As you might expect, we have a vital interest in encouraging a viable and healthly U.S. Merchant Marine industry.

After thoughtful consideration of the issues involved, Sohio stands firmly in favor of the recent DOT rulemaking allowing CDS vessels access to domestic trading opportunities in exchange for full repayment of subsidies. Similarly, we oppose current efforts to delay or significantly revamp DOT's decision in favor of full CDS payback. While the arguments on both sides of this admittedly complex issue carry considerable weight, the company believes the overall benefit of CDS payback far outweigh any potential costs.

During the past six years, there has been a demonstrated need from time to time to use CDS vessels, typically very large crude carriers (VLCCs), to ship Alaskan North Slope (ANS) crude to market. To date, employment of CDS tankers has been possible only under waivers of up to six months in duration (but not more than six months in one year) as provided under Section 506 of the Merchant Marine Act, 1936. Marad regulations specify that CDS tonnage may only be used in the ANS trade after shippers have demonstrated that available Jones Act vessels over 100 MDWT were insufficient to satisfy project short-term tonnage requirements.

It is extremely difficult to forecast accurately long-term tonnage requirements in the ANS trade. The most significant variable affecting projections is the quantity of Alaskan crude which is moved from Valdez to the U.S. East/Gulf Coast through the Republic of Panama. Relatively minor changes in production levels, import levels, and/or PADD V refinery runs will cause major changes in the volumes of ANS shipped through Panama.

Given the high level of uncertainty, Sohio believes CDS payback is needed to cover potential tonnage deficits in the years ahead. Our forecast of future tanker demand suggests there may be substantial periods of time when the Valdez fleet of Jones Act tankers of suitable size, plus CDS vessels operating under the waiver system, will be insufficient to satisfy industry requirements. The tonnage shortfall would either impede the critical flow of ANS to market, compel sizable investments which would only be required for limited periods of time, or require very high-cost and inefficient use of small ships unsuitable for this trade. Sohio believes that any of these outcomes would be contrary to the national interest.

Full CDS payback will also mean a more efficient fleet and increased competition in the domestic tanker trade, leading to lower transportation costs for Alaskan crude and ultimately contributing to the health and vitality of the U.S. economy. As the committee is no doubt award, large tankers carry crude at a lower cost per barrel than small tankers because vessel operating costs do not rise proportionately as cargo volume increases. Unrestricted access to the domestic trade for CDS vessels would result in the displacement of higher cost vessels by lower cost vessels. Fleet configuration would ultimately be determined by economies of tanker size, length of voyage, operating cost and flexibility, size restrictions, and the distribution of Alaskan crude demand at specific ports. Following a period of transition during which older, higher cost vessels would be redeployed, the most efficient carriers could then be employed to move ANS to each distinct market.

While it is impossible to project the exact market reaction to DOT's final rulemaking, we are in general agreement with their assessment that overall benefits could be substantial. More quantifiably, unrestricted payback could return close to $300 million to the U.S. Treasury if all VLCC subsidies are repaid with interest.

Lastly, Sohio favors CDS payback because it exemplifies a major policy commitment by the current administration which we strongly endorse: namely, a directive to minimize government interference in private sector affairs. We believe the free market is the most efficient arbiter of resource distribution and management, and that government involvement, while frequently invited to remedy short-term dislocations or financial injury, almost always eventually undermines the health of a free market economy if not kept in check.

In summary, Sohio believes the DOT decision for full CDS payback is in the best interest of the domestic Merchant Marine tanker fleet specifically, and the U.S. in general. We urge the committee not to prolong the debate over CDS payback, which has gone on for years, but rather to allow the rulemaking to be implemented in its current form and let the free market work to the benefit of all parties involved.

I will be pleased to answer any questions you may have.

STATEMENT OF DONALD R. BRINKLEY, VICE PRESIDENT, TRANSPORTATION, SOHIO OIL CO., CLEVELAND, OH

Mr. **Brinkley**. Thank you, Mr. Chairman.

Sohio is the largest producer of Alaskan North Slope crude oil, and we operate the largest fleet of ships engaged in this trade. We have under long-term lease, long-term charter, and a small amount of short-term charters some 30 vessels totaling more than 3 million deadweight tons.

As is indicated in my prepared testimony, we are firmly in favor of the proposed DOT rulemaking. However, acceding to your wishes, I will leave it at that, except to point out a couple of things that are our basic concerns in addressing this whole issue.

One is that there is a great deal of difficulty in determining exactly how much tonnage will be required in a given period of time to move Alaska North Slope crude oil to the lower 48 States. These difficulties include determining exactly how much production there will be on the North Slope, how much oil will be left in PADD V on the west coast, the level of imports in PADD V, the level of refining runs in PADD V, and the level of non-ANS production, because Alaskan North Slope crude oil being the last crude oil to be placed on the west coast of the United States will absorb all of these swings. These relatively minor swings can produce some pretty astonishing increases in the tonnage requirements.

We have, on a number of occasions, over the past 6 years employed CDS vessels under the waiver system to supplement our fleet, and we believe that we will be—we and the industry will be—required to do that again in the future, if we are to keep the Alaskan North Slope oil moving to market, which we firmly intend to do.

While we are in favor of the proposed DOT rulemaking procedure, we are quite happy as a charterer to look at any kinds of compromises and support anything that seems to provide the kind of objectives which we have, which is insuring that the U.S.-flag fleet has sufficient tonnage at a reasonable price, reasonable efficiency, to be able to move this crude oil.

Our analysis of the requirements for tonnage over the next few years indicates to us that the tonnage required by the industry will be in excess of that available under the current half-time regulations, and, therefore, would be in excess of anything that might be available under the compromises envisioned. In other words, we believe that a compromise that will only allow half of the CDS tonnage into the market at any given time will be insufficient for the requirements over the next several years.

We also have, of course, a continuing philosophical horror of keeping the Government in the business of establishing Jones Act capacity in this particular trade, which is so vital to us. We think that the balancing of that capacity should be left to the market.

However, with those caveats, we would, as many other of the members of this panel, support any kind of compromise that would seem to achieve the objectives that we see, the most important being the access to the tonnage and the elimination of either current or proposed uncertainties as to how much tonnage will, indeed, be available.

Thank you, Mr. Chairman.

Mr. BIAGGI. Mr. Rose.

[Statement of Mr. Rose follows:]

STATEMENT OF EUGENE ROSE, PRESIDENT, SEATRAIN LINES, INC.

Mr. Chairman, Members of the Subcommittee, I am Eugene Rose. I have been President and Chief Operating Officer of Seatrain Lines, Inc. since February, 1981. I want to thank you for the opportunity to present Seatrain's views on the Secretary's CDS repayment rulemaking and on legislation to deal with the repayment of construction differential subsidy. I also want to commend the Chairman of the Subcommittee and the full Committee for their attempts to deal with this difficult and divisive issue.

SEATRAIN

Prior to 1981, Seatrain was a company engaged in shipbuilding, international containership service, tanker operations and other activities. It was a company that had developed serious trouble. In February, 1981 Seatrain entered Chapter 11 reorganization proceedings with over $1.2 billion in debt. Over $299 million in debt was owed to or guaranteed by the United States, and secured by mortgages on five Seatrain tankers. Since entering Chapter 11, Seatrain has disposed of virtually all operations except its fleet of six large tanker vessels. Two of the vessels are 225,000 DWT tankers that have repaid their CDS and are now in the domestic trade. These vessels, especially the Bay Ridge, carry heavy debt loads, including a $50 million loan 90% guaranteed by the Department of Commerce. Seatrain also owns three 265,000 DWT CDS "Mass Class" tankers, which are secured by $94 million in Title XI debt. These vessels have been eligible to participate in the Alaska trade for periods of up to six months per year on temporary permissions under section 506 of the Merchant Marine Act.

Since February 1981 Seatrain has made payments of over $190 million in principal and interest on the debt owed to or guaranteed by the Government. It has expanded over $28 million in protecting and maintaining the government's collateral. It has done this with almost no financial assistance from the Government. The Government has been and would continue to be the principal beneficiary of a successful Seatrain reorganization.

Less than two weeks before the Secretary of Transportation announced the new rule, the Bankruptcy Court for the Southern District of New York authorized Seatrain to begin soliciting votes from creditors and stockholders to complete the plan of reorganization. Hopefully with the cooperation of the Maritime Administration and the Department of Transportation, the Seatrain reorganization will be completed, and a viable reorganized company will emerge able to continue servicing the Government debt.

Seatrain's ability to serice the Government debt was and is dependent upon being able to employ its vessels in the Alaska-Panama trade. Through 1983, the rule which regulated six month entry into the trade worked well, and Seatrain was able to keep its CDS vessels employed and meet its debt obligations. In early 1984, as the result of a single over 100,000 DWT vessel not being employed, the Maritime Administration withdraw the CDS waivers which had been granted to the three CDS VLCC's which were in the trade. Even though its CDS ships were not employed during most of 1984, Seatrain continued to make payments on all Government obligations.

Seatrain is now in the process of adapting its operations to the new realities presented by the Secretary's rule on repayment of CDS.

SEATRAIN'S POSITION ON LEGISLATION

The CDS repayment rule in more or less its present form was first proposed by Secretary of Transportation Lewis in early 1983. This Committee is all-too-aware of the controversy that has since surrounded it. Few issues in recent times have resulted in such controversy and division within the maritime industry or such vigorous disagreement about appropriate maritime policy.

Recognizing that many of the arguments of both the proponents and opponents of CDS repayment had merit, and as an operator with both CDS and domestic trade tonnage, Seatrain from the outset attempted to encourage the two contending factions to seek common ground. Particularly in the last year, Seatrain has tried to promote one compromise after another. The proposals were intended as starting points for discussion among the contending parties. They were intended to achieve many of the benefits cited by the proponents of the rules such as transportation savings, efficiency, fleet modernization and fiscal benefit to the Government, while at the same time moderating tonnage entering the trade. Unfortunately Seatrain's effort, although diligently pursued, was unsuccessful. However, we continue to believe that a compromise would offer the best solution to the industry. We also believe that a compromise would present the least risk to the Government of losses on Government guaranteed debts.

We commend both Chairman Biaggi and Chairman Jones for their efforts to find a middle ground solution. We hope they are able to succeed where we were not.

While the bills introduced by the two chairmen differ in approach, both contain some or all of the following elements which we believe are essential to a legislative compromise in this difficult area: realization of transportation savings that will result from utilization of additional CDS vessles in domestic trade: providing greater certainty to users and thereby permitting advance business planning, and avoiding lengthy proceedings; putting the CDS and domestic trade vessels on a fair and equal competitive footing; and moderating the entry of additional capacity into the domestic trade.

We believe that both the bills are intended to accomplish these objectives and that, with modification, either approach could serve as the basis for a viable compromise.

Turning first to Chairman Biaggi's Bill, we are pleased it has many points in common with one of the proposals which we advanced as a compromise. It also answers most of the objections raised to our proposal. By providing for half time repayment, it has the virtue of moderating the capacity which will be added to the trade at any one time. It also has the advantage of allowing entry in the domestic trade automatically, which is one of the requirements of a compromise solution at this time.

With reference to paragraph (2)(b)(3), we believe it important to emphasize that vessels must be available on a predictable basis to charterers. Repayment is only useful if the user of the vessel can be certain of its availability at a given time.

Second, as the Bill already has all the elements of a compromise, by limiting the repayment to half time use, we think the one year time limit should be examined.

With these modest changes, we believe the Bill would be a good vehicle for compromising the two points of view, and minimizing adverse impact on the Government.

Turning next to Chairman Jones' Bill, we believe that this Bill is intended to allow for the utilization of CDS vessels, while offering a hearing procedure for those who believe they are being injured. As we understand the Bill, a CDS vessel could operate six months in the domestic trade if the Secretary found it necessary or appropriate to carry out the proposes of the Merchant Marine Act, and could continue to operate after that if there were no findings of harm. We think it important that any such hearing be an expeditious process, similar in time to that under the current part 250 rules, and not a lengthy trial-type proceeding.

In the second phase of the proposal, an operator of a Jones Act tanker can file a notice of harm. Assuming there were a finding that a Jones Act vessel could not compete, we believe the legislation nonetheless grants the rights of the CDS vessel to operate alternate six months cycles, so long as the Secretary finds it appropriate to carry out the purposes of the Merchant Marine Act.

We have two points which we hope Chairman Jones will find helpful in considering this legislation. First, the oil companies which ship Alaska oil want to be able to be certain that chartered tonnage is available. For planning purposes, they want to be able to count on a vessel being either in or out of a trade. In 1984, when Exxon became unable to rely on the long-term availability of the CDS ships which it had chartered, it ordered two new ships. Therefore the standard for six months entry must be as automatic as possible.

As our second point, we note the *Stuyvesant* case made clear that once a vessel has fully repaid CDS, it competes on a completely equal footing as if it had been built without subsidy. This has been generally recognized. It is also true, although not generally understood, that if a vessel operates six months in the domestic trade and is idle six months, even if it received a full 50% CDS, its capital costs are just as high as an unsubsidized vessel's. It has no capital cost advantage or unfair subsidy. It must pay its entire year's debt cost in six months of operation, so it has absolutely no unfair advantage over an entirely unsubsidized vessel. If it received only

40% CDS, as did the three Seatrain CDS ships, then its capital costs are higher than they would have been as an unsubsidized ship. So we believe that any unsubsidized ship can indeed compete, except for operational factors such as size. Economy of scale should not be a basis for exclusion of a CDS vessel, or a finding that an unsubsidized vessel cannot compete.

Our comments on both bills at this point are necessarily somewhat general and tentative in nature, reflecting the shortage of time and a desire to study both more carefully and carefully analyze their legal operation and economic impact on the trade. However, the important point is that both bills offer a basis upon which to compromise. We are hopeful that other witnesses will also come forward with suggestions. For example, we understand that another compromise being suggested is that each operator be permitted to repay CDS on one vessel. That approach also merits serious consideration. We would appreciate the opportunity to work with the Committee and staff on the two bills introduced and on other suggestions that come forward as the legislation progresses.

Whichever of these proposals becomes law, or failing a compromise, if the Secretary's rule comes into force, then we strongly believe the original reason for the repayment of CDS, as enunciated in the Supreme Court case on the *Stuyvesant*, should be assured: the Government must improve or at least not damage its collateral. We believe that the Secretary's new regulation will not meet this requisite unless Seatrain is able to repay the CDS on its VLCC's.

Although the Regulatory Impact Analysis expects a $100 million positive fiscal impact from the regulation, and the House Budget Committee draft presumes $200 million, these figures will be clearly erroneous unless there is repayment on the Seatrain CDS VLCC's. In fact, using the Secretary's own figures, if Seatrain does not repay CDS on its VLCC's the effect on the Government will be to turn the proposed $100 million positive figure to $25 to $50 million negative.

Let me explain why. The Secretary predicted seven VLCC's would repay, producing $277 million in revenue. She deducted $100 million and $70 million in potential losses, for a net impact of $100 million.

She then said if only four VLCC's repay, that the revenue would be reduced by $130 million. But the analysis neglected to also take into account that $94 million additional defaults would occur, because if the three CDS VLCC's do not repay they will become of no value. So using the Secretary's own figures, if only four vessels repay, the fiscal impact will be $140 revenue, less defaults of $100 million plus $94 million, for a negative impact of $54 million.

On the other hand, if Seatrain repays on its three VLCC's, it will produce $130 million in extra revenue for the Government. It will also not have to default on the $100 million of Government guaranteed debt in its domestic trade ships or the $94 million on the CDS ships. So the Government will benefit by protecting all its collateral, for a total of over $300 million!

Permitting Title XI to finance the repayment of CDS on the Seatrain VLCC's poses absolutely no risk to the Federal Government. The Government will receive all funds for repayment, so the Government takes no additional risk whatsoever in granting Title XI for the Seatrain VLCC's. Based on the charter rates both we and the regulatory impact analysis project, the government will protect its $94 million collateral on the Seatrain CDS VLCC's, receive repayment funds of $130 million, and protect itself against the projected loss on the *Bay Ridge* and *Stuyvesant*. The total benefit to the Government is over $300 million, at no additional risk. Allowing Seatrain to finance repayment with Title XI is in keeping with the Merchant Marine Act, which makes explicit provision for Title XI to finance repayment of CDS. It follows the precedent established by MarAd. It also carries out the intent of the regulatory analysis, which noted that if Title XI were not available it would unfairly limit repayment to cash-rich companies.

Seatrain has worked long and hard to assume an orderly workout of the tanker business. We believe we have been highly successful in protecting the Government's collateral. The Government is already over $190 million better off as a result. We believe the Government would be in error not to protect its collateral by not allowing Seatrain to repay CDS through Title XI if the new regulations go into effect.

We appreciate this opportunity to testify, and again wish to commend the Chairman and Committee for their efforts.

STATEMENT OF EUGENE ROSE, PRESIDENT AND CHIEF OPERATING OFFICER, SEATRAIN LINES, INC., NEW YORK, NY

Mr. Rose. Thank you, Mr. Chairman.

I am Eugene Rose. I am president and chief operating officer of Seatrain Lines, Inc.

Seatrain is the operator of both Jones Act and CDS tonnage.

I thank you for the opportunity to comment upon the two pieces of legislation, and also on the rulemaking. I want to turn, first, to the rulemaking and make a couple of very brief comments.

The arithmetic in the rulemaking presupposes that as much as $277 million of funds will go into the General Treasury as a result of repayment, offset by potential losses up to $170 million of title XI defaults.

Seatrain, in reviewing the analysis, notes that the assumed losses relate principally to two of its vessels and gives rise to $100 million loss. What it also assumes is that, after suffering these losses, Seatrain will still be in a position to repay the CDS on three of its vessels. This assumption, we think, is erroneous.

If Seatrain is not in a position to repay on its three CDS vessels, then the amount of revenue that the Treasury receives is reduced to roughly $140 million, and the amount of potential defaults in title XI is increased by the $94 million attributable to those CDS vessels. So that, rather than $100 million positive impact upon the Treasury reflected in the RIA, or the $200 million reflected in the Budget Committee report, it is conceivable that the Treasury would suffer an immediate loss of in excess of $50 million.

We believe that the only way that the rule can work with positive result to the Treasury is if Seatrain is in a position to make repayment.

We also believe that the overriding consideration of the rulemaking, which is to put this newer, more efficient tonnage into the trade, does not work unless the Seatrain vessels repay, because three of the seven CDS ships would not come into the Alaskan trade and two LCC's that are presently in the trade, the *Bay Ridge* and the *Stuyvesant*, may be severely hampered by the ultimate demise of the company. We believe the only possible way for the rule to work is if Seatrain can repay.

We also think that, because of the various positions by both the proponents and the opponents of the rule, the proper way and the best way for the Government would be a compromise between the parties. For the last 2 years, we have diligently been trying to work compromise after compromise. Quite frankly, we have had very little success and, to a great extent, a lot of our efforts have fallen upon deaf ears. But we still believe that compromise is the best answer.

We look at both of these bills that have been offered and they look to us to be meaningful steps in the direction of compromise. We have some problems with both of them; principally, points that have been raised by other people at this table—that the repayment or waiver procedure has to be fast, it has to be quick. The repayment window, if it must be there, cannot be a short window and also there cannot be uncertainty as to whether the vessels get into the trade.

I wanted to turn back to your comments, Mr. Chairman, in regard to the title XI fund and to express our strong support of your statement regarding the title XI fund.

We have laboured for the last 5 years to work out probably the greatest risk to the Government in the fund today, the *Bay Ridge* and the *Stuyvesant*. We believe that if our *Massachusetts* class vessels are allowed into the trade and are able to secure financing, principally through title XI, that their income will be such that they will be able to supplement and keep the *Bay Ridge* and *Stuyvesant* from a potential default on the Treasury.

Our premise is that the money that would be guaranteed by the title XI fund for repayment of the three CDS vessels, would be money that would go into the Treasury, not increasing any risk to the title XI or to the Government overall, since it has received the money directly.

If the vessels work the way we believe they will, we will be in a position to continue to service the debt on all of our ships—the *Bay Ridge*, the *Stuyvesant* included—and, hopefully, there would never be a default.

In this regard, we look at the statute which authorizes title XI as being available for CDS repayment and we look at the rulemaking itself, which contemplated that companies would be in a position to rely upon title XI. To us, it is crucial that title XI financing is available to help us through this time, so that our ships can enter and fulfill the overall maritime policy of the administration and at the same time protect the title XI fund from severe default.

Thank you, Mr. Chairman.

Mr. Biaggi. Thank you very much for your expressions.

Initially, I was against any of the payback plans, but we are realists. We saw the snowball coming down the side of the mountain. In view of that, we attempted to develop some compromise.

Evidently, some people are intractable. I would say that all the members of the panel today at the table are willing to compromise. I have some realistic assessments, as contrasted to what Secretary Scocozza said. I think Mr. Mills confirms it. Even though the payback will be costly initially, there is sufficient potential profit in the plan to make it worthwhile.

Is that correct, Mr. Mills?

Mr. Mills. We hope there will be, sir.

Mr. Biaggi. Well, I am sure there will be. Otherwise, you would not have embarked on the undertaking.

That is the way it should be. We don't expect you to go into business to lose money or embark in an area to lose money.

Mr. Mills. Indeed, sir.

Mr. Biaggi. My colleague said, "Mr. Berger won't lose money." [Laughter.]

Mr. Mills. I certainly hope not.

Mr. Biaggi. We respect his ability and his business sense and his down-to-earth approach.

On the other side we do not want to see the domestics get hurt. However, recognizing what we were confronted with, we attempted to make some efforts at compromise. Apparently, domestics for the most part are against any form of compromise. When they testify, we will speak to that.

We have not received any suggestions for compromise, although there were some comments on the bills, and we appreciated those comments. I think there is a feeling that those changes can be done to your satisfaction.

Is a compromise possible or should we simply abandon the whole compromise effort and let the rulemaking take effect? Does anybody care to respond to that? There is always that alternative for this committee.

Mr. Mills. Mr. Chairman, let me take a run at that for the rest of the panel and then be corrected if I don't state it correctly.

I believe, Mr. Chairman, that there is a compromise available and possible if there are two sides willing to compromise. My friend, Mr. Bowman, has a great analogy and I won't steal his thunder, but, as I recall it, it causes me to chuckle.

Mr. Biaggi. Well, it takes two to tango.

Mr. Mills. Yes. [Laughter.]

Mr. Bowman. Well, I had mentioned that the sound of compromise was the sound of one hand clapping so far. [Laughter.]

We need some cooperation to make any progress.

Mr. Mills. If the compromise table were a ship, it would have a hard starboard list, Mr. Chairman. We're there.

We must consider the possibility of compromise in the political climate in which we exist, and the political climate in which we exist, Mr. Chairman, has that rider on the appropriations bill. It seems to me that if the other side has put their eggs in that basket, that is a terribly significant and abrupt indication of where they are going. If that is the dance, the sound, I guess we will dance.

Mr. Biaggi. I understand. Well, we will find out soon enough how they feel about it.

Mr. Bowman. May I add one thing, Mr. Chairman? I think that any compromise can occur only if both sides have something to lose by adhering to their existing, opposing lines. So far the people at this panel have been the losers over the last 5 years.

Mr. Biaggi. Mr. Bowman, I am just talking about prospectively. You have lost in a sense that you have not made the profit that you think this change will bring about, but I don't see you losing. But I do recognize that you are prepared to make less money than you would have without a compromise.

Mr. Bowman. My point, Mr. Chairman, was simply that I don't think that compromise is possible until opponents of the payback believe they have something to lose. When you ask the question of whether the rule should go forward, I think that is the only situation in which compromise can be discussed.

Mr. Biaggi. I understand.

How do you react to allowing each company to repay the CDS on only one vessel?

Mr. Oettinger. We prefer the option, Mr. Chairman, of two vessels because when one pays the CDS back on the first vessel, that can then enter the Jones Act trade with full rights, but the other vessel then becomes a relatively dead asset. These are expensive units to begin with. From our standpoint, since the corporation is the owner of two units, we are attempting to properly balance the value of both units, again consistent with the potential compromise in mind.

Mr. Biaggi. How does one vessel become a dead asset? It is still out in the other trade, isn't it?

Mr. OETTINGER. Looking at things into the next several years prospectively——

Mr. BIAGGI. There isn't any business.

Mr. OETTINGER [continuing]. There is no business.

Mr. BIAGGI. I see; well, that is the reason for this whole shift in attention.

What if we limited repayment to ships which have been unemployed for a certain period of time or percentage of time over the last 2 or 3 years?

Mr. MILLS. We don't like that option, because it seems very heavily weighted on the domestic side. They get to continue to do whatever they have done the whole time, and those of us who—for example, the Berger Group has ships coming off charter. They have been employed up until now, but they are going to come off charter and then they are going to be losing some money. Under that kind of a scenario, the heck with it—they are doomed forever to lose money while the other side continues to enjoy the benefits.

Mr. BIAGGI. Why are they coming off charter now?

Mr. MILLS. The charters have run their life. They were chartered when they were first delivered and they were term charters.

Mr. BIAGGI. So what we are doing is picking the tenderloin at different stages of the game; right? You did well when they were under the charter. If there were continued business out there, you would stay out there. Because there is not continued business out there, you are going to come and pick this apart?

Mr. MILLS. Well, "doing well" and "continued business" are two terms that I cannot really apply to some of the ships that I am referring to. I don't think breaking even is doing well. I don't think not making any money and having them in and out of layup, and then having absolutely no prospect in the future, is anything of doing well.

Mr. BIAGGI. When you consider the condition of the whole industry at this point, if you are breaking even, for some that is a win because you are down at the low ebb. When we have recovery, you will be off and flying, as contrasted to some companies that are losing money.

Mr. MILLS. Mr. Chairman, if you characterize breaking even as winning——

Mr. BIAGGI. Under certain circumstances.

Mr. MILLS. Under certain circumstances, I suppose I cannot argue with that, but we in this room are not the only people in this game. The American taxpayers, the American consumers are also in this game. By putting our ships back in and lowering the rates, increasing tax revenues, increasing the money paid into the Treasury from CDS and interest, forgiving the ODS obligations, I think there are a lot more winners out there if our ships pay back.

Mr. BIAGGI. Do you want to say something, Mr. Thomas?

Mr. THOMAS. I was simply going to comment that, in fact, it is not a question these days of making a little money or making a lot of money. It is a question out in the international trade, in fact, of consistently losing money with U.S. flag ships at the moment.

Mr. BIAGGI. OK. If we prohibited the use of title XI for repayment, could you accept the rule? I see one head nodding in the affirmative; others look puzzled.

Mr. **Oettinger**. Atlantic Richfield is not planning to use title XI funds, so we could accept the rule.

Mr. **Biaggi**. Mr. Bowman.

Mr. **Bowman**. That is also true of American Petrofina.

Mr. **Biaggi**. Mr. Mills.

Mr. **Mills**. No.

Mr. **Thomas**. I think it is probably also true of Moore McCormack. It is not absolutely necessary.

Mr. **Biaggi**. Seatrain can't.

Mr. **Rose**. There is absolutely no way that we could——

Mr. **Biaggi**. I understand, Mr. Rose.

What if we limited repayment to vessels over 100,000 deadweight tons?

Mr. **Mills**. Absolutely not, Mr. Chairman. [Laughter.]

Mr. **Biaggi**. You have your rifle honed in, don't you?

Mr. **Mills**. Yes, sir. [Laughter.]

Mr. **Biaggi**. It is claimed that the repayment of CDS with interest, as proposed by DOT, will eliminate the economic advantage of CDS operators and reduce windfall profits for domestic operators. Do you agree with that evaluation?

Do you want me to say that again?

Mr. **Mills**. Yes, please, Mr. Chairman.

Mr. **Biaggi**. It is claimed that repayment of CDS with interest, as proposed by the Department of Transportation, will eliminate the economic advantage of CDS operators and reduce windfall profits for domestic operators.

Mr. **Mills**. I think that the repayment with interest, Mr. Chairman, will certainly—the interest factor certainly makes the vessels less competitive when they go back into the trade than, for example, under the existing scheme with 6 months without interest, but, nevertheless, the repayment with interest still provides the market choice for all of the vessels represented here to pay back and to reduce considerably the profits that have been made in the trade—spread them out actually.

Mr. Bowman.

Mr. **Bowman**. I think that the committee should recognize that the interest payment mechanism in the rule is quite severe. In fact, in most cases the interest factor is two or three times the amount of the CDS itself. It is my view that that clearly makes these vessels that are entering the trade operate at a disadvantage to the existing Jones Act operators.

Mr. **Biaggi**. I think you made reference in your remarks, Mr. Oettinger.

Mr. **Oettinger**. No; I just wanted to make the comment that the term "windfall profits" I think——

Mr. **Biaggi**. It is a terrible term, isn't it? [Laughter.]

Mr. **Oettinger**. Particularly, when you try to characterize any marine business, whether it is domestic or foreign, it is inappropriate. Thank you. [Laughter.]

Mr. **Biaggi**. Mr. Snyder.

Mr. **Snyder**. Thank you, Mr. Chairman.

Mr. Oettinger, following up on the chairman's question about the potential one-ship option versus more, and your response that the one that you did not pay back would be a dead asset because there

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is no business out there for it, isn't it true that without the rule, or a compromise, or something to allow the payback, that you have two dead ships out there?

Mr. **Oettinger**. I would agree with you that the compromise that the chairman suggested may be better than what we have, but when we take a look at all the alternatives out there, I rank that very low on the list.

Mr. **Snyder**. We don't know what all the alternatives are going to be.

Mr. **Oettinger**. Well, just the alternatives that we have been talking about today: full payback plus the chairman's bill, and we have heard some other comments. I am saying there are other alternatives. When we try to do just a quick economic analysis on them, this one happens to fall lower on the list than others.

Mr. **Snyder**. In looking over some of DOT's background material, I think I recall that they indicated that 1 year or so ago Arco opposed CDS repayment. If that is correct, can you tell me why you changed your position?

Mr. **Oettinger**. Our position 1 year ago was more of being neutral, but the key point was that we wanted to insure that all Jones Act vessels over 100,000 tons were employed prior to granting CDS payback. At this point in time we have changed our position slightly, and now we are in favor of CDS payback.

Mr. **Snyder**. Mr. Mills, it has been alleged that CDS repayment will provide a windfall for the Berger Group tankers, particularly by enabling them to be bought out of their current charters in the foreign trade with proceeds available to finance the CDS repayment, thereby making them an even greater economic threat to the existing Jones Act fleet. Can you respond to that allegation?

Mr. **Mills**. Mr. Chairman, that is preposterous. I attribute it to perhaps unjustified zeal and hyperbole by those who would oppose payback.

The fact of the matter is—and I think Mr. Shapiro, for whom I am sitting today, made the offer in an open context—that if believe that is so, we will agree right here and now and I will bind the company on my authority as their counsel to turn over any windfall profits which we obtain from any charter termination payments—we will turn that over to the Government or, better yet, we will turn that over to one particular of the operators in the domestic trade now if they will agree that if there is no payback they will give us half of the profits on only one of their ships. How about that?

Ms. **Mikulski**. So moved.

Mr. **Mills**. Ma'am?

Ms. **Mikulski**. So moved.

Mr. **Mills**. You've got it, Congresswoman.

Ms. **Mikulski**. And you've got an amendment to that effect.

Mr. **Mills**. We'll take it, just as long as the other half is on, Ms. Mikulski.

Mr. **Snyder**. Mr. Mills, Mr. Shapiro's statement which was filed indicated that your company was legally required to dispose of 20 foreign-flag vessels. Is that when you entered into CDS contracts?

Mr. **Mills**. Yes, sir; CDS and ODS contracts in the early 1970's; yes, sir.

Mr. **Snyder**. He also states that some Jones Act operators use their profits to expand foreign-flag fleets. Is it possible to identify those companies?

Mr. **Mills**. Yes, sir, it is; it is quite possible. They are publicly held companies. They have annual reports that make no—it is public knowledge.

Mr. **Snyder**. Does Mr. Shapiro or your office have a list of those that they could submit for the record?

Mr. **Mills**. Yes; we would be glad to do that.

[Material retained in subcommittee files.]

Mr. **Biaggi**. Mr. Anderson.

Mr. **Anderson**. Thank you, Mr. Chairman.

Mr. Oettinger, I am going to direct my questions to you because I am a bit more familiar with your operation on the west coast than I am with some of the others.

I know you have already touched on this, but what are the benefits that you see arising from the DOT rulemaking as they relate to Arco Marine, and the entire merchant marine? I suppose I am thinking of the west coast in that regard, too. How is it going to affect us?

Mr. **Oettinger**. Mr. Anderson, basically the DOT rulemaking, when it becomes effective, it is going to provide an opportunity to use the more efficient vessels, vessels that are capable of carrying 1.5 to 2 million barrels compared to vessels that might be carrying on the order of half a million barrels, and we are talking about moving oil from Valdez to the U.S. west coast and to Panama. We are talking about moving those barrels over several thousand miles.

When one can use the more efficient vessels, the cost of transporting the oil can be decreased by a relatively decent amount. We think that this phenomenon can be characteristic of the industry and not only Arco Marine. What we have done the last few years, we have divested of our most inefficient units and they have been in most cases smaller product vessels and some of our smaller crude vessels. We have sold those vessels. We have constantly been trying to achieve the lowest transportation cost. We think in the kind of environment that we are in now that is probably got to be our No. 1 objective.

Mr. **Anderson**. Is there a danger, though, of too many vessels in the Jones Act trade business?

Mr. **Oettinger**. I think that is a possibility. It is certainly an industry that—and it was touched on by Mr. Brinkley—where you can have tremendous swings in demand and supply going from a shortage of vessels to a surplus and can certainly go the other way.

Mr. **Anderson**. Is that true in oil cargo shipping as well?

Mr. **Oettinger**. Yes, but I do want to mention that we are supportive of the free market system determining who the most efficient operators are going to be.

Mr. **Anderson**. In the reference to the two-is-better-than-one vessel discussion, I understand that you want to use these vessels to move Alaskan crude. What type of operations are these vessels currently involved in?

Mr. **Oettinger**. As I just briefly mentioned, over the last 1½ or 2 years we have had very little business for these vessels. We have

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not been as lucky as others in obtaining waivers from the Maritime Administration. The last time we have obtained a waiver was January 1984. That is of tremendous concern for us and one of the reasons that we are trying to limit or eliminate the discretion of that particular agency in future compromises.

The other aspect is that we have been fortunate to have several strategic petroleum reserve cargoes from the Persian Gulf and from the United Kingdom, but that business will be eliminated at the end of September. So we greatly see a problem and we are trying to maximize the value of those vessels, and do that in our fleet——

Mr. ANDERSON. Then these two vessels have not really been working?

Mr. OETTINGER. That is correct.

Mr. ANDERSON. What about the crew? In other words, there have not been crews working on them, either, or what?

Mr. OETTINGER. Well, we're——

Mr. ANDERSON. In other words, have they been standing relatively idle with no crew and this would mean additional employees put on the crews, added to it, or what?

Mr. OETTINGER. We have tried to balance our total fleet in terms of labor, but there could be some slight upside to it if we can get full utilization of those vessels.

Mr. ANDERSON. I know a minute ago all of you were talking about compromising. You say you are willing to reach a compromise between the DOT ruling and the two bills. I was wondering what kind of changes you were thinking of that would result in a compromise. In other words, what are you thinking about when you say, "We are willing to compromise"?

Mr. OETTINGER. Well, we mentioned that we thought that the chairman's proposed bill could very well provide a structure for us to certainly want to move forward on and want to make sure that we eliminate the discretion and we think that the interest, the compounded interest, and particularly at the rates that the Department of Transportation has put forth in their regulatory analysis, we feel are a penalty. It would not be appropriate for units that are operating only 50 percent of the time.

Mr. ANDERSON. Thank you, Mr. Chairman.

Mr. BIAGGI. Mr. Lent.

Mr. LENT. Mr. Rose, are you the only ship operator that would need title XI financing in order to repay the CDS?

Mr. ROSE. I really don't know, Mr. Lent, but I know that we cannot proceed unless title XI financing is available to us.

Mr. LENT. Have you initiated talks with MarAd on this subject?

Mr. ROSE. Yes, we have.

Mr. LENT. Can you give us some idea of what their response has been?

Mr. ROSE. Their response was that we should put in our application as soon as possible and they will consider it.

Mr. LENT. Mr. Mills, your testimony seems to state what DOT considered unlikely; namely, the repayment of CDS on the Berger Group's Panamax-sized tankers. Can those tankers operate economically in the ANS trade after repayment under the DOT rule?

Mr. MILLS. Generally, Mr. Lent, we believe they can. We believe that they can operate—while at higher rates than identical ships are able to charge, they will, nevertheless, be lower than the rates which have prevailed and are likely to prevail again in the trade without payback.

Mr. LENT. I would like to just touch on the matter that was raised by the gentleman from Kentucky earlier, the action the other day that I feel was rather unfortunate of the House Appropriations Committee, which approved the legislative language in the fiscal year 1985 supplemental bill that would prohibit the use of any funds to enforce a CDS payback rule unless the rule were to conform to statutory standards enacted at some future time.

I guess you have had an opportunity to examine that language, Mr. Mills. What is your understanding of the prohibition on enforcing the rule dealing with a payback, if Congress does not pass or has not passed that limiting language by June 6.

Mr. MILLS. Mr. Chairman, we have looked at the language and we see a number of defects in it. I must say that on initial glimpse, and given where we would like to come out on this thing, I don't think that DOT needs any money to enforce the rule. I don't think it takes any enforcement to accept a check. If it did, I suppose that might be cured by our throwing in another 10 bucks or whatever they are paying the people for accepting the checks nowadays.

We would construe the language as narrowly as we could see fit to do it. That notwithstanding, that would certainly lead to a court challenge and it would be far preferable for all involved—far preferable—for that language to be stricken.

Mr. LENT. Suppose the Congress never got around to passing any future legislation, as is contemplated in the appropriations language? What would be the legal ramification then?

Mr. MILLS. Assuming that the appropriations language would pass?

Mr. LENT. Assuming the appropriations language passes——

Mr. MILLS. Right.

Mr. LENT [continuing]. And that language, if you read the last clause of the language, contemplates Congress passing some future legislation. My question, then, is: Suppose that the appropriations language was passed but the Congress never moved forward and passed any future legislation, as is contemplated?

Mr. MILLS. Well, the first element is, of course, that it is unlikely that the appropriations bill would pass, if at all, in a time before June 7 or June 6, whichever the effective date is of the rule.

Upon June 6 or June 7, the law is that one may pay back his CDS. That is an election, and there is no approval required with respect to that.

We start there. If thereafter the appropriations language became law in its present form, then we would have some more lawyers employed defending lawsuits. I am confident that people would, absent some other compromise of course, attempt to pay back, and I am sure the people who would not want that payback would sue alleging that the appropriations act precluded that, and then we would go and we would have a district court judge, and ultimately a court of appeals, decide what that language meant.

Mr. **Lent**. How long would it ordinarily take for the DOT to act on an application for payback? In other words, we see that the rule goes into effect on the 6th of June. Even if a motion to strike this language were not successful and it somehow wound up in the final appropriation, there would be this window of opportunity that might be from the 6th of June to somewhere around the 30th of June, and perhaps even into early July. During that period it would seem to me that an applicant could make an application to the Department of Transportation to pay back its CDS subsidy with interest.

Mr. **Mills**. Mr. Lent, I don't think that there is much of an application. I think that is an overused word. I think Mr. Scocozza used it, but there is not really an application process.

You hand over a check and you tender a——

Mr. **Lent**. No, you don't necessarily hand over the check; you have a year to hand over the check.

Mr. **Mills**. Well, you certainly do, but we are talking about the actual payback. You have a year within which to hand over a check and tender a pro forma amendment to your construction-differential subsidy contract. That's it. They have to sign the amendment to the CDS contract, which gives effect to the release from the section 506 restrictions. Now that is how long it takes.

But I don't mean to diminish at all the difficulty and the process of aggregating the kinds of funds we are talking about aggregating in order to pay back. All of the companies here represented are responsible companies. They are not going to pay back just willy-nilly. Nobody keeps $40, $50, $60 million of cash in their wallet. It is going to be financed some way or another, and there are corporate decisions. This takes time to get ready to do.

I was only addressing myself to the DOT aspect.

Mr. **Lent**. Yes, but we both agree that the rule gives you a year to come up with the money?

Mr. **Mills**. Yes, sir.

Mr. **Lent**. So no one expects you to come up with the money between the 6th of June and the 25th of June, or whenever this appropriation limitation might go into effect. It would seem to me you could certainly have your papers ready on the 6th or the 7th of June and put them in, offering to make the payment within the 1-year period, as provided under the terms of the rule.

Mr. **Mills**. Well, I hope that you are correct on that. They certainly contemplate a full year within which to pay back. Whether we can bind them at an earlier period, we would certainly try.

Mr. **Lent**. I have no further questions, Mr. Chairman.

Mr. **Biaggi**. Ms. Mikulski.

Ms. **Mikulski**. Thank you, Mr. Chairman.

First, a question for the Arco group: you were originally opposed to CDS payback. I wonder why your position changed.

Mr. **Oettinger**. The environment we are operating in has changed. When one takes a position, it is not for life. I think particularly in this kind of world we have to be flexible. One can look at what Atlantic Richfield is doing, and I certainly cannot address it, but——

Ms. **Mikulski**. I wanted to know why Arco changed their position, not why the world changes. Why did you change?

Mr. **Oettinger**. Why did we change?

Ms. **Mikulski**. Yes.

Mr. **Oettinger**. We saw some potential benefits on utilizing the CDS vessels in our fleet that were not necessarily there a year or two ago. The way we configure on the west coast has changed. The environment has changed slightly on the west coast relating to tonnage.

Ms. **Mikulski**. Why did you originally embrace CDS?

Mr. **Oettinger**. Pardon?

Ms. **Mikulski**. Why did Arco originally embrace accepting CDS?

Mr. **Oettinger**. We felt that it was not at that point in time in the best interest——

Ms. **Mikulski**. No, but you originally did support CDS; is that right—having CDS and utilizing CDS?

Mr. **Oettinger**. We did not take a position on it. We got these two CDS vessels in an exchange with Gulf. We were not involved in the CDS process per se. In other words, we got the vessels and, with it, we then became involved in the CDS issue. That was in early 1982.

Ms. **Mikulski**. Did you also get ODS?

Mr. **Oettinger**. No, we have no ODS and we have no title XI.

Ms. **Mikulski**. Seatrain, weren't you once a proponent of CDS payback and have changed your position?

Mr. **Rose**. No.

Ms. **Mikulski**. I mean an opponent.

Mr. **Rose**. We have——

Ms. **Mikulski**. You were once an opponent of CDS?

Mr. **Rose**. No. We were silent in the beginning and took no position because we were and continue today, to be in chapter 11 bankruptcy proceedings——

It was just not the opportune time for us to really take a position. The ships were working. They were working toward getting out of reorganization.

We have not become an out-and-out proponent of CDS repayment. On the other hand, we have believed that the waiver rule which worked effectively through 1983 has not worked well recently and that changes are required.

We do not out-and-out favor repayment. What we have worked for and continue to hope for is compromise, so that there will be a continued predictable source of large efficient CDS tonnage in the trade to meet the requirements of the shippers.

Ms. **Mikulski**. When did you last build a ship in an American shipyard?

Mr. **Rose**. Seatrain actually was the owner of the Brooklyn Navy Yard and Seatrain itself built four of the 225,000-ton deadweight tankers. The two ships which Perofina controls, the *Brooklyn* and the *Williamsburgh*, were built at the Brooklyn Navy Yard. Our ships, the *Stuyvesant* and the *Bay Ridge*, were built at the Brooklyn Navy Yard. To my knowledge, the *Bay Ridge* is the last American VLCC that was built.

Ms. **Mikulski**. I just asked a simple question: When did Seatrain last build a ship in an American shipyard?

Mr. **Rose**. That ship, I believe, was delivered in 1980.

Ms. **Mikulski**. 1980?

Mr. Rose. Yes.

Ms. Mikulski. So you last built a ship 5 years ago?

Mr. Rose. Yes.

Ms. Mikulski. This is to the whole panel. Would you seek extending CDS repayment beyond the current 1-year period in the rule? You just think it should last 1-year? You have a 1-year window if this rule goes through. Do you think it should be permanent or should we just open the window?

Mr. Mills. If I could take a first crack at that, Ms. Mikulski, we did not seek the 1-year window. We are satisfied with the rule as it now stands with that in it. We are not now—none of us is proposing to extend that window.

If there were delaying tactics, some delays either legislatively or judicially, we might well seek to recoup that which might be lost.

Ms. Mikulski. Is that the overall sentiment of the panel?

Mr. Brinkley. I am not entirely sure whether 1 year is exactly the right number, but I do believe that there has to be a time of extinction on the opportunity. Otherwise, people will drag their feet and it will be difficult putting the pieces together.

Ms. Mikulski. So you think it should have a maximum time for entry?

Mr. Brinkley. Yes, Ma'am.

Ms. Mikulski. Then the window closes.

Mr. Thomas. We also share that view, that there should be a limit in time, and 1 year seems reasonable to us, too.

Ms. Mikulski. I would like now to move into the issue of rates. Now this would go for Moore McCormack and the Berger Group.

Everyone is saying that the rates to transport Alaskan crude will be cheaper because of CDS payback. Won't you actually have to charge more because of your debt service, since existing but older tankers have less debt on them?

Mr. Thomas. Certainly in our case we will have higher debt service, but we feel that we can still operate in the domestic trade at rates lower than some of the ships of comparable size are earning today.

Mr. Mills. I think I would have the same response, Ms. Mikulski. The rates would be lower than many rates which would prevail. We have said all along that our ships, which have identical ships already in the trade, built in the same place, same series, our ships will be more expensive than those identical ships, but still much cheaper I think than other ships which have been in the trade.

Ms. Mikulski. Have you developed any rate structures? Could you share with us what a comparison would be and how your rates would be lower?

Mr. Mills. How our rates would be lower than other vessels?

Ms. Mikulski. Yes; the ones that you will probably be displacing.

Mr. Mills. I think for the Berger vessels the breakeven will be somewhere between 11 and 11.50 per ton per month. The rates throughout the period have been as high as in excess of $20 for smaller vessels.

Ms. Mikulski. The same ones that you will be competing with? In other words, are we talking about comparing comparable vessels?

Mr. Mills. What we are talking about, Ms. Mikulski, is that our ships would carry cargoes which have been heretofore carried by less efficient vessels and smaller vessels. Add that against the identical vessel in the trade, we cannot beat it.

Ms. Mikulski. Mr. Chairman, I am not going to pursue this. It just seems to me that we have shippers who bought into the concepts of building ships with the use of subsidies. Now they want to pay those subsidies back and they want to go into something called the free market. They took no great risk. They had all kinds of subsidies, loan guarantees, breaks. Now they want to come back and they want to talk about the free market. I really do believe we are going to displace people who took enormous risks, to whom we gave a set of rules, and I really question the public policy decision that DOT is embarking on.

I have no further questions.

Mr. Lent. Mr. Chairman.

Mr. Biaggi. Mr. Lent.

Mr. Lent. I wonder if I could just follow up on the point that Ms. Mikulski has made and ask anyone on the panel: Isn't it a fact that the title XI loan guarantees were also available and utilized by the vessels that are currently engaged in domestic traffic?

Mr. Mills. Yes, of course, Mr. Lent.

Mr. Lent. So the vessels that you gentlemen represent did not derive any advantage with title XI that was not equally available to the vessels that are currently operating in the Jones traffic carrying the oil from Valdez down the west coast and into Panama?

Mr. Mills. Mr. Lent, certainly with respect to title XI, that is exactly true. The question of the subsidies, availing ourselves of the subsidies, we availed ourselves of the direct subsidies; the others availed themselves of the indirect subsidies.

Mr. Lent. Again, from the consumer's point of view of a homeowner in the Northeast who has an oil burner and is buying oil and paying $1.25 or $1.30 a gallon for that fuel, can you give me any help as to whether there will be a saving on the east coast in terms of the price of oil as a result of the CDS payback going through?

Mr. Mills. I will let the oilman handle it.

Mr. Brinkley. Congressman, the advantage to the cheaper carriage of oil will not affect the price of oil on the east coast or on the gulf coast because that price of oil is being set by the imported oil, which always makes up the last price-setting barrels of oil imported into the United States.

The advantage that your constituents should see will accrue from the fact that the net back, the cost savings to the oil companies, will produce higher net backs of Alaskan oil which will produce higher Federal revenues through taxation and taxes to the State of Alaska.

Mr. Lent. I am somewhat confused because I have read editorials in the New York Times and other newspapers when they were pressing for passage of this rule, that it was going to result in considerably lower cost for consumers in the Northeast not only of home heating oil, but gasoline and other fuel products as well.

If the present carriers are charging upward of $20 a ton—I think Mr. Mills used that figure—and the larger vessels will be able to carry that same tonnage for as low as $9 a ton, isn't that savings going to redound somehow to the benefit of the consumer?

Mr. BRINKLEY. I share your concern, Mr. Congressman. I get confused when I read the New York Times, too.

Mr. LENT. Do you mean the New York Times is wrong?

Mr. BRINKLEY. Let me try to put it in context, if I may, a little bit.

When we are talking about using VLCC's, whether they be the VLCC's that are sister ships of these CDS VLCC's in the Alaskan trade now in our service—and we have several of them—they can haul a barrel of oil from Valdez to Panama about 40 cents less than, 40 cents a barrel or a penny a gallon less than our less efficient ships, which are not small ships; they are 120,000 tons. That is the magnitude that you are talking about.

Again, the cost savings is reflected in a higher net back for Alaskan oil, which makes the oil companies more money, which the Government gets half of or, under the windfall profits tax, gets a great deal more than half of, and the State of Alaska gets increased royalty and severance.

Mr. LENT. I thank the gentleman.

I have no further questions.

Mr. BIAGGI. I have no further comments nor questions.

However, with relation to the window, I can see where you folks would think 1 year is enough, because I am sure you are prepared to move. Once that window is closed, you have it all to yourselves.

Thank you very much for your testimony. We appreciate it.

The next witness is Mr. Lee Rice, president of Shipbuilders Council of America.

[Statement of Mr. Rice follows:]

STATEMENT OF M. LEE RICE, PRESIDENT, SHIPBUILDERS COUNCIL OF AMERICA

Mr. Chairman and members of the Subcommittee, I am M. Lee Rice, President of the Shipbuilders Council of America, the national trade association representing the principal domestic shipbuilders, ship repairers, and providers of equipment and services to the industry. A copy of our membership list is attached to this statement.

We maintain our strong opposition to the Department of Transportation's rule which will allow Construction-differential-Subsidy built tanker vessels, for a period of one year, to repay subsidy and enter the Jones Act trade. We have testified previously on this matter before the Subcommittee on May 8, 1984. In addition, on March 23, 1983, we submitted comments to the Department of Transportation. Copies of these Statements are attached.

Since January 1983, the Congress has blocked promulgation of the Rule because it was found to be unsound and potentially harmful. Once again, because the DOT continues its prior course unabated, the issue is before the Congress.

Our opposition is based principally upon the adverse effect the Rule has on the national security. It is certain that:

1. The Rule will result in fewer operating, and fewer available militarily useful tankers in the U.S.-flag fleet.
2. Studies now underway will conclude that, even without CDS repayment, the number of available tankers is far below the requirements which have been determined by the Department of Defense working, at least in theory, in conjunction with the DOT. Because the Rule will deplete the U.S. fleet even further, it will force the government to acquire substantial additional tankers for the Ready Reserve Force, probably from foreign owners.
3. The Rule will, for all practical purposes, eliminate the shipbuilding market for replacement vessels for the Jones Act trade for ten or more years and as a consequence will cause the shipyard mobilization base to shrink even farther below the level of capability and capacity which must be maintained in the national interest.

4. The Rule will reduce the number of seagoing berths available and as a consequence require that the Navy organize and fund, on a continuing basis, an Active Merchant Marine Reserve to enable the Ready Reserve Force to be manned in a time of national emergency.

All significant and negative effects of the Rule upon the national security are dismissed cavalierly in the statement by the DOT which provides their analysis as to why the Rule should be implemented. They are wrong as to the facts cited, and they should be wrong in presuming that they can ignore their responsibility to maintain national security resources as required under the Merchant Marine Act of 1936.

Further, they use incorrect assumptions and facts in concluding that the shipyard mobilization base is supported by the Navy shipbuilding program and Jones Act vessel construction and repair as they would wish to have you believe.

That the Administration has ignored the negative impact on the national security in allowing the Rule to go forward is a blatant abrogation of responsibility to the American people. At this point only immediate action by the Congress in the form of legislation can gain the attention of the President. All other means of causing him to focus on a most serious problem have failed.

The only other avenue open to prevent the Rule from taking its deadly toll on our national security is to resort to the courts. Here, however, we face the difficulty that since the responsibility for the nation's security is assigned to the Executive under the Constitution, that the Courts will not likely reach a finding that the President has failed in his Constitutional duties.

Our forum for action must be this Committee.

Careful review of the facts which underlie the national security arguments which we made in opposing the Rule when it was first proposed have only enhanced their validity. The development over the last several years of the Jones Act shipping and shipbuilding markets fully support our arguments that the Rule will be very harmful to the national security.

It is undeniably true that there will be benefits to some which will result from the Rule. Others will be greatly harmed. Among these are the citizens whose security is placed in jeopardy.

We urge this Subcommittee to act in the overall national interest and ban the enforcement of the Rule as proposed. We doubt, however, that Congressional action will be effective without corollary action by the Courts.

We do, however, strongly request that this Subcommittee act promptly to prevent the Rule which now applies only to tanker vessels, from being broadened to include all vessel types. We are convinced that under present law other vessels must be given the same right. Only the Congress can act to change the law and prevent even worse long term negative effects upon the nation's security.

[Attachment]

REGULAR MEMBERS

ADDSCO Industries, Inc., Mobile, AL.

The American Ship Building Company, Tampa, FL; AmShip Division, Lorain, OH; Tampa Shipyards, Inc., Tampa, FL.

Avondale Shipyards, Inc., New Orleans, LA.

Bath Iron Works Corporation, Bath, ME.

Bay Shipbuilding Corporation, Sturgeon, WI.

Bethlehem Steel Corporation, Bethlehem, PA; Beaumont, TX; Sparrows Point, MD.

Coastal Dry Dock & Repair Corporation, Brooklyn, NY.

Dillingham Maritime Group, Portland, OR.

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Marine Power & Equipment Company, Inc., Seattle, WA.

Marinette Marine Corporation, Marinette, WI.

National Steel & Shipbuilding Company, San Diego, CA.

Newport News Shipbuilding, Newport News, VA.

Norfolk Shipbuilding & Drydock Corporation, Norfolk, VA; Norfolk, VA (2 plants); Berkeley, VA.

Pennsylvania Shipbuilding Company, Chester, PA.

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Southwest Marine, Inc., San Diego, CA; San Francisco, CA; San Pedro, CA.

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Foley, Hoag & Eliot, Boston, MA.
Hayward Industrial Products, Inc., Elizabeth, NJ.
Maersk Line, Limited, New York, NY.
ManTech International Corporation, Alexandria, VA.
McLean Contracting Company, Baltimore, MD.
McNab, Inc., Mount Vernon, NY.
Ocean Electronics, Inc., Brooklyn, NY.
Poten & Partners, Inc., New York, NY.
Seacoast Electric Supply Corporation, Rye, NY.
Standard Marine Services, Inc., Bayonne, NJ.
Sulzer Bros., Inc., New York, NY.
TechMedia Corporation, Philadelphia, PA.
Terry Corporation, New London, CT.
Tidewater Construction Corporation, Norfolk, VA.
Tomlinson Refrigeration & Supply Company, Elizabeth, NJ.

NAVAL ARCHITECT MEMBERS

Gibbs & Cox, Inc., New York, NY.
J.J. Henry Company, Inc., New York, NY.
John J. McMullen Associates, Inc., New York, NY.
M. Rosenblatt & Son, Inc., New York, NY.

ASSOCIATION MEMBERS

The American Waterways Operators, Inc., Arlington, VA.
New England Ship Repair Yard Association, East Boston, MA.
New York and New Jersey Dry Dock Association, New York, NY.
South Tidewater Association of Ship Repairers, Inc., Chesapeake, VA.
Western Shipbuilding Association, San Francisco, CA.

STATEMENT OF M. LEE RICE BEFORE THE MERCHANT MARINE SUBCOMMITTEE ON H.R. 5071, MAY 8, 1984

Mr. Chairman and members of the Subcommittee, I am M. Lee Rice, President of the Shipbuilders Council of America, the national trade association representing the principal domestic shipbuilders, ship repairers, and providers of equipment and sources to the industry. A copy of our membership list is attached to this statement.

Our opposition to the Department of Transportation's plan to permit construction differential subsidy-built vessels to repay their unamortized subsidy and enter the Jones Act trade dates back to the original publication of the proposed rule in January of last year. In testimony before this Subcommittee on March 3, 1983, we stated our opposition to the proposed rule on the ground that it would have an immediate adverse effect on our Nation's security. We explained that this adverse effect would be in two forms: first, it would result in the retirement or scrappage of many of the smaller, militarily-useful tankers presently engaged in the Alaskan North Slope oil trade, replacing them with larger tankers which are virtually useless for sealift; and second, it would forestall shipbuilding opportunities for Jones Act tankers for the next 10 to 15 years, thereby accelerating the decline of the commercial shipbuilding industry.

In the interest of brevity, we will confine our remarks to events which have occurred since this Committee last discussed the issue and add our specific comments on H.R. 5071. Our March 3, 1983 testimony is annexed to this testimony as Attachment A.

Soon after this Subcommittee's hearing on CDS payback last year, 15 members of the Committee led by Chairman Jones, Mr. Biaggi and the late Mr. Forsythe wrote to Secretary Dole asking that she withdraw the proposed rule. That letter, dated March 23, 1983 posed the problem of the national security implications of the proposed rule, and stated that a thorough analysis of the rule's impact on national security should be undertaken. Two days later, seven Senators, including four members of the Senate Committee on Commerce, Science and Transportation also wrote to Mrs. Dole to request that the national security implications of the proposed rule be studied carefully (see Attachment B).

A study of the issue has taken place, but apparently not within the Department of Transportation.

On March 28, 1983, then Deputy Secretary of Defense Paul Thayer wrote to Mrs. Dole to formally request that she not make the proposed CDS payback rules effective. Mr. Thayer stated his opposition on the basis of national security. He stated:

"The effect of this rule change would be threefold: (1) smaller, militarily useful tankers would be squeezed out of the domestic trade market by large tankers supported by the proposed rules; (2) our depressed shipbuilding industry, which has looked forward to the business created by the Port and Tanker Safety Act of 1978 would be deprived of the anticipated work it so badly needs; and (3) a windfall profit would be provided to a few major companies with CDS-built tankers under charter."

Mr. Thayer's letter enclosed a memorandum to Mrs. Dole from then Assistant Secretary of the Navy George Sawyer which further explained the national security problems resulting from the proposed rule. Mr. Sawyer also cited the adverse effect on shipbuilding as well as the reduced capability for sealift which would result from the CDS payback rule.

Both Mr. Thayer's letter and Mr. Sawyer's memorandum are enclosed as Attachment C and Attachment D to this statement.

More recently, the National Security Advisor Robert C. McFarlane has expressed a similar view, that the national security could be harmed, in a letter to Senator Sam Nunn. This letter is enclosed as Attachment E.

On the basis of the analysis by DoD, our own and that of other industry groups, we continue our opposition to permanent CDS repayment for tankers to enter the Jones Act fleet. Further, the shipyard mobilization base would be supported if a permanent ban were enacted against the practice of continual grant of waivers to allow CDS-built vessels into the trade. However, since this is unlikely to be done, we feel strongly that waivers be granted only those situations where it can be shown that insufficient tankers capacity exists and the the shortage will continue for an extended period.

H.R. 5071 anticipates a continued refusal by the Department of Transportation to recognize the defects of its CDS payback scheme and to publish a permanent regulation in the near future. We agree that concern is well placed. We support the goals of H.R. 5071. Nevertheless, we suggest that it be strengthened to ensure that DOT cannot ignore national security concerns.

H.R. 5071 would set out three criteria under which an application for permanent CDS payback would have to be evaluated after a hearing on the record that: (1) existing service in the domestic trade is inadequate; (2) the vessel cannot find employment in the foreign trades for extended periods; and (3) with written concurrence of the Secretary of the Navy, the transfer of the vessel would not adversely effect the national security.

We suggest a stronger national security test should be applied. This test should ensure that the sealift capabilities of the U.S. merchant marine are not reduced by any large vessel displacing smaller, more useful vessels. Therefore, we suggest that the third test be rewritten to state that:

"(3) With the written concurrence of the Secretary of the Navy, that the addition of such vessel would not cause loss of employment of any vessel meeting military usefulness criteria which is not fully provided by the vessel seeking permission, and will not otherwise adversely affect the national security."

Under the proposed text, there is greater assurance that sealift capacities would not be adversely affected by the application.

We appreciate this Subcommittee's continued attention to this difficult problem of national security. We remain astonished that the Administration continues to disregard the national security effects of proposed maritime rule implementation. Only by congressional vigilance can we hope to maintain some semblance of national mobilization capability.

[Attachment A]

STATEMENT OF M. LEE RICE BEFORE THE MERCHANT MARINE SUBCOMMITTEE, MARCH 3, 1983

I am Lee Rice and am appearing before the Committee on behalf of the Shipbuilders Council of America. The Council has submitted extensive and detailed comments in its full testimony pertaining to the Notice of Proposed Rulemaking issued by the Department of Transportation regarding CDS repayment for tanker vessels seeking to obtain unrestricted Jones Act privileges. I request that the Committee fully review this statement and that it become a part of the record as well as my summary statement.

Other witnesses have dealt with the devastation that the proposed rule will have on the Jones Act fleet. I will, in this presentation, focus on its highly negative effect upon the shipbuilding and shiprepair industry and the national security.

In addition, however, our views of the failures of the Department of Transportation in its considerations of the CDS issue are deemed to be important to the work of the Committee.

It is apparent that the Department of Transportation, functioning as the lead agency under authority granted by the Congress and as delegated by the President of the United States to carryout through the Maritime Administration the administration of the Merchant Marine Act of 1920 and the Merchant Marine Act of 1936, both as amended, proposes to and/or has:

(1) Abrogated its duties under these acts and in contravention of the stated policy of the President, to provide the Nation with an adequate U.S. flag merchant marine and domestic shipyard base to serve its needs,

(2) Used faulty logic and incomplete or unreliable data in the development of the proposed rule,

(3) Ignored the effect that a change of policy in regard to the export of ANS crude oil would have upon the proposed rule, a policy which will be debated and determined by action of the Congress in regard to the expiration of export restrictions for ANS crude oil contained in the Export Administration Act which expires in September of this year,

(4) Based arguments which underpin the advocacy position of the Department on unacceptably narrow grounds in seeking to enhance the position of the Government at the expense of a limited group of the citizenry, and

(5) Incorrectly concluded that the proposed policy change can be evaluated under Executive Order 12291, Federal Regulation Requirements, dated February 17, 1981.

Our explanation and discussion of these failures is presented in detail in the full testimony.

The Department argues throughout its paper in support of the proposed rule that efficient vessels are better. They do not define efficient. However, a reading of their material makes it clear that efficient equates to larger and less modern vessels which they contend will offer lower transportation cost per DWT. We question whether this definition is either meaningful or desirable. We note that not a single vessel of those built with CDS which would be expected to enter the ANS trades and displace smaller and "less efficient" vessels would be found to be useful for service as naval auxiliaries in a national emergency. The contrary is true of the smaller "less efficient" vessels the Department is prepared to see scrapped. The Merchant Marine Acts of 1920 and 1936 are both premised upon the value of a commercial merchant marine to support the national security. The Department neglects this fundamental underpinning of our national security base when it cavalierly dismisses this entire issue. Our newest, most efficient and well equipped vessels, are vessels recently completed or under construction for Jones Act trades. These same vessels are those most negatively affected by the proposed rule and are at the same time those most highly useful to support the security interests of the Nation. The role of military usefulness of these vessels is most valuable when these vessels are a part of the active operating commercial fleet. Does the Department argue that these vessels in layup or in the reserve fleet as a result of debt defaults will make them more useful to the national welfare? This is patent nonsense!

The Administration has not given meaningful consideration to the adverse consequences to the national security that results from its present policies. The direct results of which are that the shipyard mobilization base is reduced below a defined minimum level and that the Nation is set upon a path which eliminates our capacity to build commercial vessels. The policy position that U.S. shipowners should buy vessels from foreign sources, that CDS must be eliminated and the failure of the Administration to develop a sound shipping promotional program has this result. The demise of this important national asset, the capability to build commercial ships, is hastened by the proposed rule. In the immediate future, the last international trading vessel either being built or on order will be completed. Within a short time thereafter, the group of Jones Act vessels currently under construction will also be delivered. Thus, commercial shipbuilding in this Nation will be at an end. This is the policy of the Administration, but is it the correct policy? The Merchant Marine Act of 1936 requires that a shipbuilding capability be maintained to meet the requirements of the national security in time of emergency. Reliance upon foreign shipyards to fulfill this requirement is not lawful. It is well known that the naval shipbuilding program neither is an acceptable substitute for a capability to build commercial vessels nor is it sufficient to maintain an adequate shipyard mobilization base. It is our view that the Administration has de facto changed the laws of the nation and continues to be, at best, irresponsible in this regard.

In the case of the new rule proposed to be established, the Department of Transportation, seeks to further this irresponsibility. In its material supporting the new rule, it cites the fact that a significant part of the Jones Act fleet is old and will likely not be modified to comply with the Port and Tanker Safety Act. (Aside, we note, that this tank fleet which is assigned to be scrapped—is far younger and in better repair and service condition than is the National Reserve Fleet upon which high reliance is placed for breakout and use as a primary component of sealift under defense mobilization planning.)

U.S. shipyards can expect, within the next few years, that a potential replacement program of Jones Act tonnage will occur. With the availability of the CDS vessels which buy their way into the trade with Department of Transportation support, however, the occurence of such a market will be significantly postponed. Indeed, if the market occurs, it may occur after U.S. shipyards have lost or abandoned the ability to build these needed vessels. Is this part of the overall strategy of the Administration—the complete abrogation of the Jones Act?

Shipbuilders have had a substantial market for tank vessels to serve the Jones Act. Prior to the 1970 amendment to the Merchant Marine Act of 1936, construction of vessels for Jones Act trading was the only basis for any tanker vessel construction. Likewise after the mid-70's, the market essentially returned to the condition existing pre-1970. Is this a market that should be disrupted or abandoned? In our formal testimony we show the importance of the Jones Act as a shipbuilding market. Since 1976, 49 Jones Act tankers have been delivered or are under construction. These vessels aggregate over 4 million dwt of capacity and include the best, most efficient and militarily useful vessels available. The data also shows that with the exception of two vessels being built with CDS funds at present to release two equivalent vessels from life-charter to the Military Sealift Command for service in the Jones Act trade, no market has existed for CDS built tankers since 1975. Should the adverse effect upon the shipbuilders and their suppliers be ignored in the promulgation of the new rule? We think not!

The Jones Act market has produced over $2 billion in shipbuilding contracts and has supported many thousands of jobs in our industry. Ships being built to trade as Jones Act vessels are vital to our military security and the national welfare. Nowhere do we find that the views of the Department of Defense or the National Security Agency have been considered in this matter.

We understand that principal proponents of the proposed new policy will not be in their present roles in the near future. Secretary Dole is newly in office and in the process of replacing her principal subordinates. Further, the full effect of the rule upon the shipbuilding and shipping industries will not be immediately apparent. Do we then excuse those now on the scene for past errors? How do we reach those who will have irrevocably harmed the maritime industry and the national security for just retribution? A laissez-faire approach will be applauded with certainty by the Soviets and others who would damage the national security.

In summary, we believe that the Department of Transportation seeks to impose narrow and ideologically based objectives by administrative fiat. It seeks to protect the interest of the government at the expense of a small segment of the citizenry. All this without public debate or hearing on a matter which is of high importance to the national security. Once promulgated, reversal or correction of the damage caused by the proposed rule, which will destroy the Jones Act fleet as a viable element of our economy and as an efficient element of our national security, will be very difficult if not impossible. In our judgment, reliance upon comment upon a proposed rule where the process does not allow the give and take of full investigation and inquiry and where the views of the maritime experts of the administration, the Maritime Administration, and the Maritime Subsidy Board, would not be developed in public, constitutes an arrogant display of indiscretion. We strongly suggest that the Department of Transportation maintain the status quo and if it is deemed desirable that a change of policy be effected, that it be done by amendment to the Merchant Marine Acts of 1920 and 1936 whereunder the full ramifications of the change can be placed before the public through the full legislative process.

We believe that the Department of Transportation rather than promote a huge oversupply of tonnage in the Jones Act trade, should, if it has any interest in supporting the shipbuilding industry, immediately cease the grant of waivers which allows CDS tonnage into this trade and seek to limit, by law, entry by waiver in only the gravest of national emergencies situations. Both our industry and the national security would benefit—at no cost to the government.

We cannot agree that the Department of Transportation should be allowed the deception of destroying an efficient private market—the Jones Act fleet and the shipbuilding and shiprepair industries who are its suppliers—under the false guise of deregulation. The shipping and shipbuilding industries see the promulgation of the proposed rule as the worst kind of government interference in a functioning and efficient market heretofore largely immune from government administrative intrusion and error.

We implore this Committee to prevent this travesty and to demand a full accounting.

A fundamental problem continues under the present Administration. The problem is that no one other than the President himself is accountable for insuring that maritime policy and administration is consistent with its innate linkage with the nation's security. Our policy is that both the nation's vital sealift and shipbuilding capacity are to be provided by private ownership and to be sufficient in quantity to meet our needs. Thus, every change of policy or administrative interpretation of policy must be measured as to the effect upon the private ownership of these national assets—shipping and shipbuilding capacity. In regard to the proposed rule which is being discussed, be assured that no one with proper authority and responsibility has been required to determine that the negative impact of the rule on the national security is desirable.

Will the President certify to the Congress that this rule and those policy directives which fix the manner of administration of our maritime laws do not negatively affect our national security? There is no mechanism that requires such certification. Consequently, the question will be ignored and remain unanswered. Thus, essential elements of our national security, already far too weak, are dissipated with apparent approval and encouragement from the White House.

[Attachment B]

U.S. SENATE,
Washington, DC, March 25, 1983.

Hon. ELIZABETH H. DOLE,
Secretary of Transportation, Washington, DC.

DEAR MADAM SECRETARY: We are greatly concerned by the Department of Transportation's proposed regulations on payback of construction differential subsidies ("CDS"). The proposed regulations would establish a new policy which would adversely affect our nation's economy and security.

According to the January 31, 1983 notice, the objectives of this proposal are to: (a) replace smaller tankers in the Alaskan North Slope oil trade with larger CDS-built ships presumed to be more efficient; (b) reduce the cost of transporting Alaskan oil; and (c) benefit the Government financially by recapturing CDS funds and reducing exposure under Title XI ship mortgage guarantees. We question whether the proposal will accomplish these objectives.

The "bumping" of smaller ships in favor of larger ones will not increase efficiency because many of the smaller ships are the newest, most efficient tankers available. Similarly, there is no assurance that the use of larger ships will lower the cost of transporting the oil; it may simply raise the profits of the ship's operators.

The supposed financial benefit to the government is equally illusory. Instead of increasing revenues to the Treasury or reducing Title XI risks, it merely shifts money from one pocket to another by allowing new Title XI guarantees to be issued to repay CDS. It also may result in the default of other Title XI loans on the many smaller ships whose future operation is jeopardized by this proposal.

Furthermore, it is apparent that the significant, adverse effects on the shipbuilding and ship operating industries, as well as our national security, have not even been studied in the preparation of this proposal. These issues concern us greatly.

As you are no doubt aware, President Reagan's Executive Order 12291 requires extensive economic analysis of any proposed regulation which is likely to affect the economy by at least $100 million annually. In a recent hearing before a Committee of the House of Representatives, Deputy Assistant Secretary Swinburn testified that these regulations would "cut-off" shipbuilding for the affected trades. This alone would result in a loss of over $250 million per year to shipbuilders. At least another $50 million per year would be lost to each involved ship operator. We urge you to follow the guidelines of Executive Order 12291, and conduct a complete analysis of these regulations before they are implemented.

Secretary Swinburn's testimony contained the startling admission that no review of the effect on our nation's security had been done. This proposal's certain adverse effects on the many smaller vessels which may be retired and which may be vital to the national security, must be throughly studied and reviewed by the Department of Defense before these regulations take effect.

In view of these problems with this proposal, we urge you to withdraw the proposed rule and appoint an interagency task force to study the far reaching economic and national security implications of this proposal.

Sincerely,

RUSSELL LONG.
J. BENNETT JOHNSTON.
WENDELL H. FORD.
PAUL TRIBLE.
JOHN WARNER.
THAD COCHRAN.
HOWELL HEFLIN.

[Attachment C]

THE DEPUTY SECRETARY OF DEFENSE,
Washington, DC, March 28, 1983.

Hon. ELIZABETH HANFORD DOLE,
Secretary of Transportation, Washington, DC.

DEAR ELIZABETH: The purpose of this letter is to request that the Department of Transportation not enact the Construction Differential Subsidy (CDS) Replacement proposal contained in your Notice of Proposed Rulemaking (NPRM), Federal Register (Volume 48, No. 21, p. 4408, of 31 January 1983).

Currently, CDS built tankers, as authorized by MARAD can participate in Jones Act Trade only to a maximum of six months annually. It is my understanding the proposed rule would lift all restrictions on Jones Act trading by CDS tankers whose subsidies had been reimbursed. The effect of this rule change would be threefold: (1) smaller, militarily useful tankers would be squeezed out of the domestic trade market by large tankers supported by the proposed rules; (2) our depressed shipbuilding industry, which has looked forward to the business created by the Port and Tanker Safety Act of 1978, would be deprived of the anticipated work it so badly needs; and (3) a windfall profit would be provided to a few major companies with CDS built tankers under charter.

The Navy's specific concern is the detrimental effect of accelerated small tanker retirements on our ability to resupply overseas forces in the event of war. Nearly half of our wartime shipping requirements, in terms of tonnage to be shipped, must be carried in tankers between 6 and 80 thousands DWT, with coated tanks to permit carriage of refined product. Larger tankers, the type supported by the proposed rules, are of limited value for military deployment and support purposes. As a result of the changes in petroleum product distribution systems, including shorter routes, greater use of pipelines, and other inland surface modes, the commercial requirement for smaller domestic oceangoing tankers has been steadily reduced. Application of the technical provisions of the Port and Tanker Safety Act will further accelerate the retirements of these tankers.

I fear that the proposed ruling to allow large tankers a greater share of domestic trade will greatly exacerbate an already dangerous trend toward small tanker extinction. I have asked the Assistant Secretary of the Navy, Shipbuilding and Logistics to provide a more detailed explanation of our concerns.

Your assistance in this matter is greatly appreciated.

Sincerely,

PAUL THAYER.

[Attachment D]

DEPARTMENT OF THE NAVY,
OFFICE OF THE SECRETARY,
Washington, DC, March 23, 1983.

MEMORANDUM FOR THE SECRETARY OF TRANSPORTATION

Subject: Construction Differential Subsidy Repayment; Total Repayment Policy, 46 CFR Part 276; Notice of Proposed Rulemaking.

With reference to your notice of Proposed Rulemaking (NPRM), Subject as above, contained in the Federal Register (Volume 48, Number 21, at page 4408, dated 31 January 1983), the Department of the Navy desires to comment on the proposed rules.

The Navy has viewed the declining health of the U.S.-flag merchant marine with grave concern. The major element of this concern has been the reduced capability of our merchant fleet to support our national defense requirements under contingency situations, particularly where the U.S. must act unilaterally and still support our private sector requirements.

We anticipate that nearly one-half of our contingency shipping requirements, in terms of tonnage to be shipped, would be in militarily-useful tankers. A militarily-useful tanker is defined as between 6 and 80 thousand DWT with coated tanks to permit carriage of refined product. Larger tankers, the type supported by the proposed rules, are of limited value for military deployment and support purposes.

Even without the adoption of this proposal, as a result of the changes in petroleum product distribution systems including shorter routes, greater use of pipelines, and other inland surface modes, the requirement for smaller domestic ocean going tankers has been reduced. As a result of the application of the technical provisions of the Port and Tanker Safety Act of 1978 to these ships in 1986, the retirements of these tankers will be acelerated beyond the rate which would normally be anticipated.

This proposal would further enlarge and accelerate that loss with at least an additional 20 tankers affected. Any deliberate actions taken as a matter of policy which effectively reduce the number of militarily-useful tankers in trade will not be helpful to our national defense posture.

An additional adverse national security impact will result from this proposal. Our depressed shipbuilding industry which has looked forward to the business created by the Port and Tanker Safety Act will not get the anticipated work it so badly needs. The Navy's combatant ship and sealift enhancement programs are not sufficient to maintain the private yards necessary for a diversified mobilization base. Given the declining private order book, the prospect for yard conversion work as well as new construction will be inhibited, if not extinguished, by a rule which would permit unrestricted domestic trade qualification by Construction Differential Subsidy (CDS) payback.

It appears to Navy that, in addition to adversely affecting our national security, the proposed CDS payback will result in little, if any, direct monetary benefit to the government; will be a breach of faith with the operators in the Jones Act Trades; and will result in a windfall to a few major companies who presently have CDS built tankers under charter.

As a result of the vessel retirements which would be occasioned by the CDS payback, Navy understands that MARAD has estimated that the title XI loan guarantee exposure of the government could be as high as $440 Million. If applications for CDS repayment are received for all eligible tankers, the unamortized Construction Differential Subsidy principle repaid will be $470 Million, plus interest.

The current Jones Act Trade operators who have Title XI exposure would be defaulting on non-Construction Differential Subsidy vessels. By foregoing CDS, these operators had acted in good faith, relying upon the operating and financial protection of the Jones Act. Your former Secretary, Drew Lewis, speaking for the Administration on 20 May 1982 and 5 August 1982, reaffirmed support for the sanctity of Jones Act and existing cargo preference laws. And, the President has affirmed his support for the domestic trades. The proposed rulemaking would arbitrarily and rapidly reverse this position at a time when the domestic tanker market is already under great pressure.

In summary, the proposed changes would not assist in national defense, and in practice would be detrimental because useful-sized clean product ships would be displaced by less useful large, crude carriers.

Recognizing the dynamic nature of the tanker trades, both in domestic and international commerce, the Navy recommends that the proposed NPRM continue the present practice of allowing temporary qualification of limited duration with full pro-rata CDS payback (including interest), and only in those situations dictated by tanker undercapacity.

George A. Sawyer,
Assistant Secretary of the Navy,
(Shipbuilding and Logistics).

[Attachment E]

The White House,
Washington, DC, November 9, 1983.

Dear Senator Nunn: Thank you for your letter concerning Construction Differential Subsidy (CDS) repayment, and its impact on our fleet of US flag militarily useful tankers. Please excuse the delay in responding to your letter, but my staff has been working on the issues you have raised.

There is no doubt that America has entered into a period of potentially dangerous shortages in terms of the available US flag fleet of militarily useful commercial vessels. Our nation has always counted on adequate commercial vessel availability to serve as the "fourth arm of defense" if conflict should come and hence the requirement to ship massive amounts of war material across the oceans. Given the Navy's broad missions of sea control, power projection involving the Marines and strategic deterrence, we cannot and should not try to create a Navy controlled transport fleet to solve this additional problem. Of course, the decline in our merchant fleet is aggravated by the steady decline in our shipbuilding base. Unlike WWII, we cannot expect in any future conflict to be able to build more vessels than those lost.

The answer to this serious defense problem, I believe, must have three components. They are: maintenance of a superior Navy in order that our merchant fleet not be attrited by a foe in war; the NATO wide merchant fleet-sharing agreement which gives us access to NATO country vessels in the event of conflict; the maintenance of our current merchant fleet at its existing level in order that we may be prepared for a possible unilateral contingency.

The specific issue you raise regarding CDS payback strikes at the center of the need for us to maintain our current fleet of militarily useful tankers (i.e., approximately 80,000 tons and below). As you stated in your letter, the Deputy Secretary of Defense and the Assistant Secretary of the Navy for Shipbuilding and Logistics have put forth strong arguments to the Department of Transportation opposing CDS payback on the grounds that such action would harm our defense capabilities.

We too have these concerns and will continue to search out all ways that we can support the preservation of the US flag fleet in this and other cases.

Sincerely,

ROBERT C. MCFARLANE,
National Security Advisor.

COMMENTS PERTAINING TO THE NOTICE OF PROPOSED RULEMAKING ISSUED BY DEPARTMENT OF TRANSPORTATION (DOCKET NO. 78; NOTICE NO. 4) SUBMITTED BY SHIPBUILDERS COUNCIL OF AMERICA, WASHINGTON, DC, MARCH 23, 1983 (REVISED)

PREAMBLE

The Shipbuilders Council of America (SCA), whose members are shipbuilders, shiprepairers, and suppliers to the industry of both services and materials and equipment, has studied the Notice of Proposed Rulemaking which proposes to amend 46 CFR Part 276 which sets forth the Department's policy in considering requests for repayment of construction-differential subsidy (CDS), as authorized under the provisions of the Merchant Marine Act of 1936, as amended. The proposed change of policy importantly impacts both the national welfare and the national security. Further, it has a major and direct impact on the shipbuilding industry.

SCA has concluded the Department of Transportation, functioning as the lead agency under authority granted by the Congress and as delegated by the President of the United States to carry out through the Maritime Administration the administration of the Merchant Marine Act of 1920 and the Merchant Marine Act of 1936, both as amended, proposes do and/or has:

(1) Abrogated its duties under these Acts and in contravention of the stated policy of the President, to provide the nation with an adequate U.S. flag merchant marine and domestic shipyard base to serve its needs,

(2) Used faulty logic and incomplete or unreliable data in the development of the proposed Rule,

(3) Ignored the effect that a change of policy in regard to the export of ANS crude oil would have upon the proposed Rule, a potential for change which will be debated and determined by action of the Congress or lack thereof in regard to the expiration of export restrictions for ANS crude oil contained in The Export Administration Act which expires in September of this year,

(4) Based arguments which underpin the advocacy position of the Department on unacceptably narrow grounds in seeking to enhance the position of the government at the expense of a limited group of the citizenry, and

(5) Incorrectly concluded that the proposed policy change can be evaluated under Executive Order 12291, Federal Regulation Requirements, dated February 17, 1981.

Further, SCA is convinced that the Executive Branch of the government does not understand either the fundamental importance that a viable, strong and capable shipbuilding industry represents to the Nation's security or the Nation's policy under which this national asset is to be provided and maintained. President Reagan in 1980 both developed and signed a statement of basic maritime policy which made clear that an adequate domestic shipbuilding industry is a part of the Nation's security system. To date, however, President Reagan has not established nor assigned responsibility within the Administration for the measurement, recording and projection of the future capacity and capability of the shipbuilding industry. Nor is any government Agency or Department explicitly charged with the responsibility to maintain this asset at an adequate level of functionality consistent with defined national needs.

Thus, no one other than President Reagan himself is directly accountable for insuring that maritime policy and administration thereof is consistent with its innate linkage with the Nation's security. The Department of Transportation is, however, charged with the administration of those very laws, cited above, which set maritime policy. Such policy is that both the Nation's vital sealift and shipbuilding capacity are to have a substantial domestic base, are to be provided by private ownership and are to be sufficient in quantity to meet the Nation's needs. As indicated above, there exists no mechanism under which these needs are reviewed, analyzed and established or responsibility for maintenance of shipping and shipbuilding assets assigned other than loosely by the administration of maritime policy under the purview of the Department of Transportation.

To serve the President, who has retained to himself responsibility for maintaining adequate sealift and shipbuilding resources, it is essential that the Department of Transportation obtain such requirements from military logistic experts and those charged with responsibility for the Nation's strategic planning for war and national emergency since the Department is neither expert nor responsible for these matters. Having obtained such information, then, and only then, can the Department examine and measure rationally the effect of any change of policy or administrative interpretation of policy as to the effect upon the private ownership of the Nation's vital assets—shipping and shipbuilding capacity.

In regard to the proposed Rule which is the subject of these comments, Deputy Assistant Secretary Swinburn has testified that no review of the adverse effect upon the national security has been made. Prudence would seem to dictate that this should be a matter of highest priority rather than an afterthought. Undeniably, the national security will be affected. The Proposed Rule must stand the test of acceptability in this regard.

STATED PURPOSE OF THE PROPOSED RULE

Following the 1970 amendment of the Merchant Marine Act of 1936, the policy of the Maritime Administration was to encourage the investment by shipowners in tank vessels—intended for commercial use in general international trade. These vessels were, in general, financed by a combination of CDS grants and Title XI debt guarantees given under programs administered by the Maritime Administration. In a substantial number of these ship purchase contracts, vessel charters of sufficient length and at acceptable rates were required to support the economic viability of the investments in accord with then existing government policy. In all of the investment decisions made by owners of these vessels, the expected vessel-lifetime trade was the international movement of bulk commodities. No owner can demonstrate any other intent. Additionally, the government accepted inherent risks of the market as to Title XI guarantees based on the vessel charters or market expectations upon which economic viability was established.

History teaches that the change in world market conditions for the shipping services that can be provided by the vessels constructed under this program has resulted in unprofitable operations for vessel charterers and owners. They, however, are not alone. Hundreds of other vessels in the world tanker fleet, both owned and chartered by U.S. citizens and foreign nationals, are in like circumstances. Only because the government has financial involvement in these vessels have they been singled out to receive extraordinary relief. The relief mechanism proposed is a financial "bail-out" of selected owner/charterers and through this "bail-out," protection of the government's risk at the expense of other vessel owners and the shipbuilding industry. In regard to the risk to the government under the Title XI program, the government has been paid by collection of fees for every guarantee issued to accept this risk. It is at best callous that the government now seeks to avoid its risk by a change of policy.

Department of Transportation records, as presented in support of the proposed Rule change, correctly identify the vessels purchased with CDS funds. They have also correctly identified those vessels whose owners or charterers will most benefit from the proposed "bail-out."

The arguments presented in support of the legal right of the Maritime Subsidy Board to allow the payback of CDS and thus qualify the vessel for unrestricted Jones Act privileges rely upon the decisions of the courts in litigation relating to the Seatrain vessels "Stuyvesant" and "Bay Ridge." We believe that the authority defined by the courts rests with the Maritime Subsidy Board and therefore we question why the Department of Transportation has found it necessary to usurp authority to promulgate the proposed new Rule. We, also, believe that the Department of Transportation in extending the authorities defined in the limited scope of the "Stuyvesant" and "Bay Ridge" issues to allow repayment of CDS to a selected class of vessels in utter disregard for the financial impact on a broad group of the citizenry and upon the overall well-being of the national security is intent upon making a gross error.

The Department of Transportation states that the purpose of the new Rule is to provide improvement in the economic health of owners of the CDS vessels following repayment of CDS through the expected profitable employment in the protected Jones Act trade—admittedly at the expense of the economic well-being of the owners of other vessels to be forced out of the trade as a result. The objectives are stated to be:

(1) Recapture of CDS funds to the Treasury which funds would be used in maritime promotional programs.

(2) Reduction in the potential of calls upon the government for guarantees of debt repayment, purchased by the borrowers.

(3) Reduction in the cost of transportation of ANS crude.

(4) Replacement of older and smaller tankers by more *efficient* CDS built tankers. (emphasis added)

ANALYSIS OF THE STATED PURPOSE OF THE PROPOSED RULE

The stated objectives of recapture of CDS funds is at best a shallow deception. The record of the Administration in developing a meaningful maritime promotional policy is highly disappointing. The CDS program has been eliminated, Title XI financing limited, and the ODS program is being curtailed and eliminated wherever possible. There is no guarantee, whatsoever that any effort would be made to use these funds for other maritime purposes or promotion. Indeed, for this to occur would require that the Administration propose increased budgets to the Congress; an event deemed highly unlikely. Further, it is by no means clear that the cost to the government of the proposed Rule will not exceed the CDS funds repaid. Indeed, the harm to the national security may be beyond measure.

The reduction in exposure of the government under Title XI guarantees by callously shifting risk to a selected class of vessel owners by the device of a policy change evidences a police-state mentality of its proponents. It is argued that Title XI guarantee calls would be reduced because the CDS vessels using repayment privilege would find gainful vessel employment while vessels without Title XI guaranteed financings would be idled and scrapped. Even if this were the likely result, it flys in the face of fairness and the basic purpose of the program itself. The purpose of the Title XI program is to cause U.S. flag vessels to be built and maintained in the fleet and available for national security purposes. It is apparent that the Department of Transportation seeks to avoid risks by deceit and subterfuge and in contravention of the purpose of the program.

Further, the Department has made a grievous error in its presumptions in regard to the affected vessels. The vessels most likely to be negatively affected by the proposed Rule are recently built vessels and vessels presently under construction for entry into the Jones Act trades. Many of these vessels have been financed using Title XI guarantees. These vessels because of the time of building are the highest cost vessels in the Jones Act trades within their competing classes. Therefore, they must receive a high capital factor in vessel charter hire, if they are to remain economically viable as investments. The "bumping process" which the Department expects to occur, will occur since the ANS movement will be greatly over-tonnaged. The "bumping process" will move older vessels into competition with new or undelivered vessels below 80,000 DWT. No analysis is made, nor is any consideration given to the increased Title XI risk associated with reduction in trading opportunity for this highly important class of vessels. The value of these vessels as contrasted with the CDS vessels will be dicussed later as it relates to the national security.

Another major error of logic is also made by the Department when it argues that those vessels under 80,000 DWT which are displaced from ANS trades can find gainful employment in other trades. They also state that vessels constructed with CDS of size less than 80,000 DWT would not repay CDS to enter Jones Act trades. Since business opportunities for the latter vessels in international trade are nearly nonexistent, and if Jones Act trade is available for vessels displaced from ANS trades, clearly the CDS built vessels would also seek to enter this trade. Logic falters at this juncture because the Department also states that CDS vessels of less than 80,000 DWT would not seek to repay CDS because financial expectations for such vessels would be poor. Poor for the CDS vessels but by some unexplained magic good for the ANS trading Jones Act vessels which are displaced by the proposed rule.

The Department argues that allowing the CDS built vessels into the ANS trade will reduce the cost of transportation and benefit consumers. We agree that excess tonnage capacity will reduce transportation costs during the period in which independent owners seek survival through rate warfare. Since, as the Department states, a large part of the transportation capacity is controlled by the owners of ANS crude, their costs will not be reduced. Any cost reduction will redound to the benefit of the shipper. The price of refined products to consumers is not affected in a major way by the cost of ANS crude but rather by the price of imported crude and products. Perhaps the government may find marginal benefit through a higher windfall profit tax collection but the consumer not at all. If such an increase in the receipts of the government are a hidden objective, it should be stated.

The Department argues throughout its paper in support of the proposed Rule that efficient vessels are better. They do not define efficient. However, reading of their material makes it clear that efficient equates to larger vessels which will offer lower transporation cost per DWT. We question whether this defintion is either meaningful or desirable. We note that not a single vessel of those built with CDS which would be expected to enter the ANS trades and displace smaller and "less efficient" vessels would be found to be useful for service as naval auxiliaries in a national emergency. The contrary is true of the smaller "less efficient" vessels the Department is prepared to see scrapped. The Merchant Marine Acts of 1920 and 1936 are both premised upon the value of a commercial merchant marine to support the national security. The Department neglects this fundamental underpinning of our national security base when it cavalierly dismisses this entire issue. Our newest, most efficient and well equipped vessels are vessels recently completed or under construction for Jones Act trades. These same vessels are those most negatively affected by the proposed Rule and are at the same time those most highly useful to support the security interests of the nation. The role of military usefulness of these vessels will continue for the vessel life; if they have an operational life. Does the Department argue that these vessels in layup or in the reserve fleet as a result of debt defaults will make them more useful to the national welfare? This is patent nonsense.

THE DEMAND FOR TRANSPORT OF ANS CRUDE

Although the Department of Transportation does not state the basis for its conclusions about further demand for transport of ANS crude, we must conclude that they have evidence that through-put of the Trans-Alaskan pipeline is to increase in the near future. We question that this is factually supportable. In a world where crude is in excess of demand, and where selling price is falling; what incentives exist for investment needed to increase production or for the strategic desirability of more rapid drawdown of ANS reserves?

Further, we believe that the Administration has in preparation a policy presentation under which it will advocate the export of ANS crude upon expiration or amendment of The Export Administration Act of 1979. This being the case, or at a minimum, until the issue is finalized, ability to project the transporation requirement for ANS crude cannot be made with realism. Therefore, it is, at best, foolhardy to promulgate a new Rule which will have far reaching impact until the issue of transport demand is determined with greater precision.

We are unalterably opposed to the proposed new Rule. However, it is also appropriate to comment on the proposed policy that only unamortized CDS be repaid, which we believe constitutes a major conceptual error and indicates a lack of knowledge by the Department. Repayment of unamortized CDS only is based on the vessels having been engaged in the international trade for a significant portion of "vessel life," defined as 20 years. We find no rational basis for the presumption that vessel life for vessels above 80,000 tons should be regarded as 20 years. In 1993, for example, the class of CDS built 265,000 dwt vessels, which aggregate 1,325,000 dwt, will have an average age of 16.8 years. Will replacement vessels be purchased for delivery in 3 years? Obvioulsy not, unless the crude reserves of Alaska will provide trading opportunities until at least 2016. This is believed to be unlikely. Therefore, a much more likely prospect is that these vessels will undergo life extension procedures which give them a useful life of at least 30 years, a period consistent with ANS reserve depletion. It is also highly pertinent that a large number of the CDS vessels were lease financed. At delivery, each owner established a vessel life of at least 30 years to obtain lease financing. Why now is it then proper to use 20 years as vessel life? The entire class has an established useful life of at least 30 years.

Should not, then, the owner be required to repay the original CDS grant in full—that is if a prime objective is CDS recapture and assuming that the vessel will replace other vesels now employed and which enjoy profitable rates. The increased vessel amortization cost resulting from full repayment of CDS will not increase the required rates beyond the point where the vessels are uncompetitive. Such costs are consistent with price of 6 month waiver entry into the trade today.

If CDS vessel owners really believe that the ANS market is secure, they should be willing to repay CDS fully,[1] in cash and without Title XI guaranteed borrowings, plus interest. If not, the Department of Transportation market projections will indeed be proven to be faulty. The owners of the CDS vessels are seeking extraordinary relief. Fairness dictates that they pay for this relief.

EFFECT ON THE SHIPBUILDING INDUSTRY

The Administration has not given meaningful consideration to the adverse consequences to the national security that results from present policies. The direct results of which are that the active shipyard mobilization base is reduced below a defined minimum level and that the nation is set upon a path which eliminates our capacity to build commercial vessels. The policy position that U.S. shipowners should buy vessels from foreign sources with CDS eliminated and the failure of the Administration to develop a sound shipping promotional program has this result. The demise of this important national asset, the capability to build commercial ships, is hastened by the proposed Rule. In the near future, the last international trading vessel either being built or on order will be conpleted. Shortly, the group of Jones Act vessels currently under construction will also be delivered. Thus, commercial shipbuilding in this nation will be at an end (excepting whatever construction may occur on the Great Lakes because of physical contraints). This is the policy of the Administration, but is it the correct policy? The Merchant Marine Act of 1936 requires that shipbuilding capability be maintained to meet the requirements of the national security in time of emergency. Reliance upon foreign shipyards to fulfill this requirement is not lawful. It is well known that the naval shipbuilding program neither is an acceptable substitute for a capability to build commercial vessels nor is it sufficient to maintain an adequate shipyard mobilization base. It is our view that the Administration has de facto changed the laws of the nation and continues to be, at best, irresponsible in this regard.

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[1] CDS repaid in accord with 6 month waivers would constitute partial repayment.

In the case of the new Rule proposed to be established, the Department of Transportation seeks to further this irresponsibility. In its material supporting the proposed new Rule, it cites the fact that a significant part of the Jones Act fleet is old and will likely not be modified to comply with the Port and Tanker Safety Act. (Aside, we note, that this tank fleet—which is assigned to be scrapped—is far younger and in better repair and service condition than is the National Defense Reserve Fleet upon which high reliance is placed for breakout and use as a primary component of sealift under defense mobilization planning.)

If the CDS vessels are allowed to repay CDS and enter the Jones Act, as proposed, surplus tonnage will exist in the Jones Act trade for an extended period. A period far longer than would occur with expected retirement and scrappage under normal conditions. U.S. shipyards can expect, within the next few years, that a potential replacement program of Jones Act tonnage would occur. With the availability of the CDS vessels which buy their way into the trade with Department of Transportation support, however, the occurrence of such a market will be significantly postponed. Indeed, if the market occurs, it may occur after U.S. shipyards have lost or abandoned the ability to build these needed vessels. Is this part of the overall strategy of the Administration—the complete abrogation of the Jones Act?

Shipbuilders have had a substantial market for tank vessels to serve the Jones Act. Prior to the 1970 amendment to the Merchant Marine Act of 1936, construction of U.S. flag vessels for Jones Act trading was the only basis for any tanker vessel construction. Likewise after the mid 70's, the market essentially returned to the condition existing pre-1970. Is this a market that should be disrupted or abandoned? The following table shows vessels delivered in the years following 1975 and includes the 1983 and 1984 vessels on order. In this Table the "Bay Ridge" and "Stuyvesant" are included as Jones Act vessels. It is also noted that the CDS vessels shown as 1983 and 1984 vessels are to replace vessels under life charter to the Military Sealift Command with Jones Act privileges and therefore, in reality, should be classed as Jones Act tonnage.

The Table clearly shows that the Jones Act market has been of high importance to shipbuilders whereas the CDS market from a practical point of view has not existed in the period after 1976 since vessel orders were placed earlier. Should the adverse effect upon the shipbuilders and their suppliers be ignored in the promulgation of the proposed new Rule? We think not!

	Jones Act		CDS	
Year	Number of vessels	Vessel dwt (1,000's)	Number of vessels	Vessel dwt (1,000's)
1976	3	78	10	1,088
1977	7	729	6	728
1978	8	1,098		
1979	5	866	1	792
1980	2	220		
1981	6	227		

Year	Jones Act Number of vessels	Jones Act Vessel dwt (1,000's)	CDS Number of vessels	CDS Vessel dwt (1,000's)
1982	[1]8	516		
1983 (to be delivered)	[1]7	400	1	34
1984 (to be delivered)	3	131	1	34
Total	49	4,265	19	2,676

[1] Includes three wrecked ships reconstructed in 1982 and one being reconstructed in 1983.

We understand that the principal proponents of the proposed new policy will not be in their present roles in the near future. Secretary Dole is newly in office and in the process of replacing her principal subordinates. Further, the full effect of the Rule upon the shipbuilding and shipping industries will not be immediately apparent. Do we then excuse those new on the scene for past errors? How do we reach those who will have irrevocably harmed the maritime industry and the national security for just retribution? A laissez-faire approach will be applauded by the Soviets and others who would damage the national security.

Moreover, the Department of Transportation's January 31 notice of proposed rulemaking states, without explanation, that this proposal is not considered to be "major" as defined by Executive Order 12291 (see 48 Federal Register 4410).

Under Section 1(b) of E.O. 12291, a major rule is one which is likely to result in:

"(1) An annual effect on the economy of $100 million or more;

"(2) A major increase in costs or prices for consumers, individual industries, Federal, State, or local government agencies, or geographic regions; or

"(3) Significant adverse effects on competition, employment, investment, productivity, innovation, or on the ability of United States-based enterprises to compete with foreign-based enterprises in domestic or export markets."

It is submitted that the proposal is more than likely to result in the events described in E.O. 12291, and that the likelihood is demonstrated not only in this submission, but in DOT's proposal itself.

a. The proposal is likely to have an annual effect on the economy of $100 million or more

Over the past 7 years, an average of 5 tankers per year have been built in the United States for the Jones Act domestic oil trades (see tables above). The average cost of each of these ships is approximately $53.6 million. In the event that this proposed regulation is implemented, the opportunity to build new ships for that trade will be terminated for 10 to 15 years. On an annual basis, this would mean a loss of revenue to the shipbuilding industry of over $265 million per year.

In addition, we have been advised informally that most of the companies operating smaller Jones Act tankers, which are most likely to be affected adversely by this proposal, each expects to lose between $10-$15 million in after-tax income each year for the next five years. Assuming on the basis of the Appendix to the proposed Rule that there are at least five companies which would thus be affected an additional $50 million per year in terms of income to ship operators must be added to the likely effect of this proposal, for a total of at least $315 million per year lost to the economy.

b. The proposal will have significant adverse effects on the shipbuilding industry

The Department of Transportation denial that this proposal is a "major" one under E.O. 12291 is belied by the proposal itself. At 48 Federal Register 4412, DOT makes the confusing statement that:

"With regard to the possible impact of the proposal on shipbuilding, the entry of CDS-built tankers into the domestic trades might, in fact, reduce the demand for new tankers in the Jones Act fleet. Nevertheless, this same industry is the primary beneficiary of the CDS program which contributed to the construction of these tankers, and the economic benefits to be derived from the use of these tankers exceeds any temporary dislocation to the industry which might result from their employment."

Apparently, DOT has forgotten two important facts: first, there is no CDS program now to stimulate new construction; and second, because Jones Act tankers have been a mainstay of commercial ship construction in the United States, elimination of markets for them will cause a major disruption of the industry. It is not clear, but DOT apparently implies, that the commercial shipbuilding industry, having benefitted in the past from the now extinguished CDS program, must now forego survival by having its non-CDS business essentially terminated indefinitely by government edict improperly pursued.

Since the loss of Jones Act tanker construction will deprive the shipbuilding industry of over $265 million in business per year, it necessarily follows that the portion of that revenue which would have been used for investment, improvement of productivity and innovation, and, indeed, the employment of shipyard workers, will not be available. In a commercial shipbuilding market near extinction, this is a significant adverse effect.

Under E.O. 12291, there is no requirement for an absolute determination of a significant adverse effect, only that it is likely. Clearly, this proposal is likely to have a tremendous impact on the shipbuilding industry in terms of future business opportunities for commercial ship construction. On the basis of the virtually certain impact on shipbuilding and ship operation, it is clear beyond peradventure that this is a "major" proposal under E.O. 12291 which must not be implemented until the terms of that Order are satisfied.

If the Department of Transportation is truly willing to fulfill its responsibility to maintain an adequate national shipbuilding capability, it should, rather than propose that the Jones Act market be flooded with excess tonnage, do just the opposite. It should propose to the Congress, and aggressively support, amendment to the Merchant Marine Act of 1936 to limit the 6-month waiver rule and to allow waivers only under the most extreme cases of national emergency. Of course, it could also accomplish this by not granting the stream of 6-month waivers which have become the norm. If the grant of waivers were terminated, shipbuilders would have a small—but meaningful—market and our national security assets would thereby be enhanced.

Under normal circumstances, we would not suggest the need for legislation in regard to the question of waiver. However, in view of the presently proposed Rule, which shows that investment by vessel owners for Jones Act trading, can at the government's whim be affected in the extreme, we believe that owners must have long term assurance of a stable market without government interference before investment will occur.

The Administration seeks to spend billions in increased defense monies. No government funds are required to obtain a significant benefit to our national security when Jones Act vessels are built. The problem, now, as it has been for many years, is that no one other than the President is held responsible for maintaining an adequate sealift capacity and an adequate national shipbuilding capability.

In the Preamble to these comments, we stated that maritime policy presumes that commercial markets will be such that private owners will purchase and operate vessels which will form our Nation's merchant marine reserve, a reserve to be called upon to serve as naval auxiliaries and support vessels in a national emergency. Policy further presumes that vessels will be purchased from U.S. shipyards in sufficient quantity to insure that an adequate shipbuilding capacity is maintained also.

In regard to tank vessels alone, we know of no analysis of trading patterns of liquid cargoes which takes into account the dramatic changes that have occurred in the Jones Act trades in the past decade. Prior to 1970, Jones Act vessels were built in numbers to participate in the coastwise movement of crude oil and petroleum products. Largely due to the extensive development of pipeline distribution systems and the increased use of oceangoing barge vessels, this market no longer exists as a major commercial opportunity.

With the completion of the ANS pipeline, an alternative commercial market developed which employed many existing vessels and stimulated the construction of a substantial new fleet. This market has been affected by other forces—the entry by waiver of CDS vessels and the completion of the across-Panama-pipeline. Commercial forces are such that transportation of ANS crude from Valdez to either the West Coast or to Panama is dominated by large crude carriers which are not useful as naval auxiliaries. Thus, the only remaining market for those vessels, which are of highest value to our national security, is the northbound leg of ANS crude delivery—Panama to the Gulf or East Coast. National policy should seek to preserve rather than destroy this market. Indeed, needed are additional markets where this class of vessel can enjoy lasting trade expectations and, thus, will be kept operative and replaced in the future. These markets must offer long term opportunity if private ownership is to occur. If such markets do not exist, the Nation's reliance upon private ownership of militarily useful tank vessels to serve the Nation's needs and partly through construction of these vessels to maintain an adequate shipyard mobilization base and construction capability will be misplaced.

FINAL COMMENTS

The Department of Transportation seeks to impose narrow and ideologically based objectives by administrative fiat. It seeks to protect the interest of the government at the expense of a small segment of the citizenry. All this without public debate or hearing on a matter which is of high importance to the national security. Once promulgated, reversal or correction of the damage caused by the proposed Rule which will destroy the Jones Act fleet as a viable element of our economy and the national security, will be very difficult if not impossible. In our judgment, reliance upon comment upon a proposed Rule where the process does not allow the "give and take" of full investigation and inquiry and where the views of the maritime experts of the Administration—the Maritime Administration and the Maritime Subsidy Board—are not developed in public, constitutes an arrogant display of indiscretion. We strongly suggest that if it is deemed desirable that a change of policy be effected, that it be done by amendment of the Merchant Marine Acts of 1920 and 1936 where under the full ramifications of the change can be placed before the public through the full legislative process.

The Department of Transportation should not destroy an efficient private market—the Jones Act fleet and the shipbuilding and shiprepair industries who are its suppliers—under the false guise of deregulation. The shipping and shipbuilding industries see the promulgation of the proposed Rule as the worst kind of government interference in a functioning and efficient market heretofore largely immune from government administrative intrusion and error.

Clearly, the negative impact of the proposed Rule upon the Nation's security, its negative impact upon our presumption—expressed as policy in the Merchant Marine Acts of 1920 and 1936—that commercial markets will exist to stimulate owners to invest in vessels and that owners will purchase these vessels from U.S. shipyards and thus maintain an adequate shipyard mobilization base; far outweigh the meager benefits argued to accrue to the government and to an even lesser extent to the Nation. Thus, the proposed Rule must be rejected and the Department of Transportation dedicate its efforts to the preservation of our vital maritime interests in shipping and shipbuilding.

STATEMENT OF M. LEE RICE, PRESIDENT, SHIPBUILDERS COUNCIL OF AMERICA, WASHINGTON, DC

Mr. RICE. Thank you, Mr. Chairman.

I appear today representing the shipbuilding industry, of course, one of those most affected parties in this whole proceeding. We have been consistent throughout this whole debate as to a position. We have opposed the rule. Not only have we opposed the rule, but we have and continue to urge legislation that would ban not only the rule, but any waiver ships from entering the Jones Act fleet.

Nevertheless, we understand the realities of life. What we would urge upon you are five fundamental points today in dealing with a compromise, if that is your bent, as it appears to be:

The first is the issue of the national security. We cannot dismiss that so cavalierly, as we believe the DOT has done. Their material supporting their rule is filled with inaccuracies and errors of fact on the national security issue. I would like to make four points on the national security and then move on to my fifth point, if I may.

First, it is our judgment the rule will result in fewer operating and fewer available militarily useful tankers in the U.S.-flag fleet. I think that is a given.

Second, studies now underway in the Department of Defense will conclude that, even without CDS repayment, the number of available tankers is far below the requirements which have been determined to be, working with the DOT, at least in theory, to be necessary.

Because the rule will deplete the U.S. fleet further, it will force the Government to acquire substantial additional tankers for the Ready Reserve Force. In all likelihood, they will have to reach into the foreign market.

Third, the rule, for all practical purposes, will eliminate the shipbuilding market for replacement vessels for the Jones Act for 10 years or more. I think you just heard the panel here indicate that essentially every ship is going to come into the market.

The result of that will be that it will shrink the shipyard mobilization base even farther below the level required to be maintained in the national interest.

Fourth, the rule will reduce the number of seagoing berths available and, as a consequence, require the Navy, as they are now planning to do, to organize and fund on a continuing basis an active merchant marine reserve to enable the Ready Reserve Force to be manned in a time of national emergency.

None of these points, in our judgment, has been properly dealt with in leading up to the rule and need to be considered.

Further, it is our judgment that in any compromise legislation or legislation that you are going forward with, you need to do one important thing—to ban the application of CDS repayment to the dry cargo fleet because we think that will be the next step. We do not see that it can be avoided if you allow the tanker fleet in, and we think that you should include in any legislative endeavor a ban of dry cargo CDS repayment for entry into the Jones Act fleet.

Thank you.

Mr. Biaggi. We recognize that you have always opposed the rulemaking. Yet, without congressional action, it will become effective June 6. Is there any compromise you could support? If not one offered, is there any one you would like to suggest?

Mr. Rice. We are in a very difficult position to put forward a compromise between ship-owning parties. We do not like to put ourselves in as an expert.

Our view would simply be any compromise you gentlemen work out should be crafted to have the minimum effect on the national security. That is the fundamental issue that we want to argue. We feel that any compromise must take that into consideration.

Mr. Biaggi. Staff is inclined to take advantage of your presence to talk about American shipbuilding, but today we are talking about a very narrow issue. You have addressed it from a mutual concern. I am not so sure that the pro and con positions would question whether national security should be jeopardized. I am sure we all would agree that it should not. That is an important factor. I share some doubts about DOT's assessment in that regard, too. I assure you we will go into it a little bit further.

Mr. Lent.

Mr. Lent. I just have two questions for Mr. Rice.

How much maintenance and repair work might the admission of subsidized vessels create for shipyards?

Mr. Rice. It is our view that since a lesser number of ships will be trading in the Alaskan trade and in the Jones Act, the volume of business will go down sharply.

Mr. Lent. What about potential new construction? What would the effect be?

Mr. Rice. We think for 10 to 15 years—because we really believe that essentially all the ships that have the opportunity will pay and come in—that we will not see any Jones Act construction.

Mr. Lent. I thank the gentleman.

I have no further questions, Mr. Chairman.

Mr. Biaggi. Ms. Mikulski.

Ms. Mikulski. Mr. Chairman, I just have a few questions for Mr. Rice.

I am pleased that he focused on the national security issues, something I know the Chair has had longstanding interest in and has held hearings on our sealift capacity.

The Independent Tankers Association, Mr. Rice, commissioned a study from Deloitte, Haskins & Sells, which you heard me raise earlier. They said that the U.S. shipbuilding industry could lose over 6,800 jobs from the implementation of this rule and 1,200 in the seafaring trades. Could you comment on what you think the impact of this rule would have on the commercial shipbuilding market in terms of jobs?

Mr. Rice. Well, as I indicated, we think it essentially wipes out the tanker market for the foreseeable future. I have not had the chance to read carefully, nor have I seen, the final study that Deloitte, Haskins, Sells has done, although they did consult with me as they were putting the study together. So I am in agreement with them on their methodology and the basis on which they arrived at the estimate that there would be 6,800 jobs lost as a consequence of the promulgation of the rule.

Now that is a mixture of jobs in the shipbuilding industry directly and the first tier supplier industry. They were less brave than I would as a multiplier—I think that many more jobs throughout the industry will ultimately be lost with that.

Ms. Mikulski. You think that 6,800 jobs is the minimum we will lose?

Mr. Rice. Correct.

Ms. Mikulski. That it will expand not only in other years, but also through its multiplier factor?

Mr. Rice. Yes; through the multiplier effect, I think the number is low. Their methodology used the first tier.

Ms. Mikulski. You talked in your testimony about the negative impact this rule would have on our sealift capacity. Just to flush that out a little bit, could you tell me how many ships in the effective U.S.-controlled fleet would be useful for sealift purposes?

Mr. Rice. Well, the Department of Defense has defined a number of roughly 66 vessels in the U.S.-controlled fleet that are militarily useful. Of that number, my memory tells me there are roughly 40 tankers that they count as militarily useful.

Ms. Mikulski. Are there enough that would sail under American flag to meet that sealift capacity?

Mr. Rice. Well, I am certainly not an expert in that issue. I share with you your earlier expressed very grave concern as to the availability of those vessels. I personally make a different argument.

If our Defense Department can identify 66 vessels within the total U.S.-controlled fleet that are useful to us in a time of a military emergency, so can the Russians. I have said, if I had their treasury and if I knew when I wanted to, I could essentially charter that entire fleet and have it in the Black Sea at any point in the future.

Therefore, it is not only an issue of whether Liberia would allow the ships to serve us, but whether or not they would be available because of a strategy developed by the Russians.

In the Department of Defense there is no one who tracks where those ships are, who they are chartered to, or where they are going. It would not be a very difficult thing, in my judgment, to do.

Ms. MIKULSKI. If they were planning a major military offense, all they would have to do is get into the charter market——

Mr. RICE. It would be quite easy.

Ms. MIKULSKI [continuing]. Either directly or indirectly through client states——

Mr. RICE. They are a very major charterer right now. Make no mistake about it.

Ms. MIKULSKI. Mr. Rice, I think you have answered my question. Thank you.

Mr. BIAGGI. Thank you, Mr. Rice.

The following panel opposes CDS repayment: Sanford V. Schmidt, manager of Chartering and Industry Relations, American Trading Transportation Co.; Francis X. Gallo, vice president of Victory Carriers; Jack Goldstein, vice president and chief economist, Overseas Shipholding Group, representing the American Institute of Merchant Shipping; and Michael Klebanoff, president of American Maritime Association, director and chairman of the board of OMI Corp.; accompanied by Joseph A. Klausner, Esq., counsel for the American Maritime Association.

Mr. Schmidt.

Mr. SCHMIDT. Chairman Biaggi, would you permit me to defer my remarks to Mr. Goldstein?

Mr. BIAGGI. Mr. Goldstein.

[Statement of Mr. Goldstein follows:]

STATEMENT OF JACK GOLDSTEIN ON BEHALF OF AMERICAN INSTITUTE OF MERCHANT SHIPPING

The American Institute of Merchant Shipping (AIMS) is a national trade association representing 24 U.S.-flag shipping companies which own or operate approximately 11 million deadweight tons of tankers, dry bulk carriers and other oceangoing vessels engaged in the domestic and international trades of the United States.

Three of our members, ARCO Marine, Inc., Standard Oil Company of Ohio and Moore McCormack Bulk Transport, Inc. are not in agreement with the position of the American Institute of Merchant Shipping on this particular matter.

The new rule of the Secretary of Transportation will strike with special force upon independent owners of modern tanker tonnage who have invested over a billion dollars in the coastwise trade within the last decade.

For some reason, the government authority charged by law to know all about shipping appears to believe that the subsidized fleet contains the most "efficient" ships under our flag. The truth is that class by class, the coastwise ships in the Alaskan trade are younger, more modern and safer than the corresponding subsidized vessels that are being allowed to enter. The older and smaller ships that are loosely talked about have largely disappeared in the last three years under the pressure of an old-fashioned shipping depression superimposed on a competitive transportation shift in the form of the trans-Panama pipeline. These purely commercial developments were enough to cause scrappings and other deletions throughout the domestic fleet approaching two million tons. Such older tonnage as remains active in the Alaska trade belongs mostly to the oil companies, and therefore, according to the Secretary's report, is not likely to be pushed out.

What will be pushed out is the independent fleet of modern tankers.

Taking the 1984 fleet on the Secretary's basis, what she calls the full-time equivalent of about 5.6 million dwt was employed in the trade; about 40%, or the full-time equivalent of 2.2 million tons, was chartered in by the ANS producers, who supplied the remainder themselves. If the subsidized VLCCs and only six Panamax tankers of 90,000 tons transfer, they would add more than that amount to the fleet, something above 2.3 million dwt.

Nor would this effect by any means be limited to smaller ships. The Secretary herself expects the two Seatrain VLCCs (originally built with subsidy) to be forced out, as well as the equivalent of three in the 100,000-140,000 ton range, and 14 in the sizes below 100,000 dwt. This is without reference to the two new Exxon VLCCs that will arrive next year, of which her paper does not take account. In fact, it may be said with assurance that every chartered vessel in the trade will be forced out, regardless of size.

This demonstrates a stark fact. The rule has been perpetrated upon a trade that does not need additional tonnage. It is still overtonnaged after a severe shake out. And there are no alternative markets for unsubsidized tonnage. This was the trade for which they were built. Mr. Klebanoff has told you the rate levels to which the Secretary herself believes the market will fall. The financial consequences require no embellishments.

We believe these consequences are not what Congress intended when it directed the Secretary of Transportation to develop and maintain an American merchant marine. We therefore ask you to re-establish the basic direction of the shipping laws, upon which a whole industry relied in building this fleet.

[Attachment]

AMERICAN INSTITUTE OF MERCHANT SHIPPING

MEMBER COMPANIES

Amerada Hess Corporation.
American Trading Transportation Company, Inc.
Amoco Transport Company.
Arco Marine, Inc.
Chevron Shipping Company.
Coscol Marine Corporation.
Diamond Shamrock Corporation.
Exxon Shipping Company.
Hvide Shipping Incorporated.
Interocean Management Corporation.
Keystone Shipping Co.
Maersk Line, Limited.
Mobil Oil Corporation.
Moore McCormack Bulk Transport, Inc.
OMI Corp.
OSG Bulk Ships, Inc.
Phillips Petroleum Company.
Sea-Land Corporation.
Signet Marine Group, Inc.
Standard Oil Company (Ohio), The.
Sun Transport, Inc.
Texaco Inc.
Union Oil Company of California.
Western Hemisphere Corporation.

STATEMENT OF JACK GOLDSTEIN, AMERICAN INSTITUTE OF MERCHANT SHIPPING

Mr. GOLDSTEIN. Thank you, Mr. Chairman.

I appear here today for the American Institute of Merchant Shipping as well as my own company. The institute has consistently opposed the CDS repayment rule and continues to stand against the rule, although three of our member ships—*Arco, Sohio,* and *McCormack*—appear today as proponents.

I have submitted testimony for the record and have a few responses to the remarks made by DOT and others as well.

The issue before the committee seems to be a complex one. Arguments can be raised on both sides that seem to be equally convincing, but when the thin facade is stripped away, Mr. Chairman, we find that every single argument of the proponents of the Department of Transportation rule has little or absolutely no validity.

As we have heard today, the basic positions of DOT and the proponents revolve around the following issues:

First, very casually, it is suggested that the Government should get out of shipping; that this is a form of deregulation. Mr. Chairman, this will be the first time of deregulating an unregulated industry. There is no regulation. There has been none. There is free entry. There are no controlled rates. There is no conference. There is fierce competition.

Second, Mr. Chairman, the rule is proposed to foster competition, to increase our economic efficiency, it says. In a competitive market, which it is already prior to the rule, we will have a more competitive market, it says, but in a competitive market, Mr. Chairman, prices are set competitively.

DOT has suggested that because of the rule rates will go down to break-even levels for all ships. This is absolute poppycock. In the competitive market the most efficient vessels earn a profit, less efficient vessels may break even, the least efficient vessels lose money and go out of business. That's how it works.

We have heard today that several of these VLCC's already paid back subsidy in 1978 and 1980. Did the rates collapse? Did it go down to break-even levels? No; those ships, to the extent they were more efficient, earned a larger profit than less efficient vessels. The market did not break.

What breaks the market, what causes the rates to collapse, simply is overtonnaging. Too much tonnage, people compete with each other, rates collapse. They do not drop to break even; they drop well below break even.

Third, we have been listening to the fable for 3 years that our fleet is composed of rust buckets, that the only ships to be affected are antiques. Well, while the proponents were building about 30 subsidized vessels in the 1970's, our industry without Government subsidy was building close to 90. Close to $5 billion was invested without subsidy.

Fourth, we have heard that this is a modern fleet, the CDS fleet; this is a highly efficient fleet, much better than anything available in the domestic trade. More nonsense. With the exception of four small product carriers which happen to be owned by Mr. Klebanoff's company, every one of the CDS vessels is economically obsolete. It is obsolete in the foreign trade; it is obsolete in the domestic trade. Why? They are all steam tankers.

No owner, whether in the domestic trade or in the foreign trade, will build a steam tanker again. There are several dozen vessels in the domestic trade which have been built which are diesel vessels.

Fifth, the next story is that the Government will realize substantial fiscal benefits from the payback. We have heard a number of $277 million, representing unamortized subsidy and interest from

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the seven VLCC's as against the potential loss from the dissolution of Seatrain, which mentioned it owns three of the seven ships.

Mr. **Biaggi**. We will have to recess for a few minutes until we finish our vote on the floor.

[Recess taken.]

Mr. **Biaggi**. The committee is called to order.

Mr. Goldstein.

Mr. **Goldstein**. Thank you, Mr. Chairman.

Mr. **Biaggi**. Mr. Goldstein, would you hold for just a minute?

[Pause.]

Mr. Goldstein.

Mr. **Goldstein**. Thank you, Mr. Chairman.

As we left off, I was on the question of the Government's fiscal benefits. I indicated that, from the public testimony, we had the possibility of an in-flow of funds from the payback of about $277 million and the potential offsetting loss from problems created for Seatrain. There is another issue that has not been addressed.

The rule assumes that the vessels indeed will be displaced, but fails to take into account what that means. In my view, virtually every chartered ship now employed in the Alaska trade would be displaced if the seven VLCC's repay subsidy. These ships in total have a debt exposure in title XI approaching $1 billion. Now, for the life of me, I don't see how those owners can be expected to repay the title XI mortgages with interest while their ships have been put out of service by the rule. It is ridiculous.

There is another claim made. These ships, these subsidized ships, are going to have to pay back a lot of money in subsidy, a lot of money in interest. They are going to be more expensive than our ships in most cases. Therefore, we have a situation which the agency has called equal footing. Everybody will be on the same competitive position. Nonsense. It's not true.

These people accepted subsidies, got charters in the foreign trade, and are being given now an option, not a requirement but an option, to repay subsidy and compete with us. That is what we call a second bite at the apple. We don't have that second bite. We are committed to the domestic trade.

Mr. **Biaggi**. You are making the arguments. We know the arguments. We know your arguments quite well.

If you remember, initially we supported your position most vigorously. We opposed the whole payback situation. But now we are talking about another scenario. We are talking about a rule that will go into effect June 6. We are trying to work out some kind of compromise.

Why don't you talk about the bills? You can give us all the arguments back and forth. We know the other side of the argument; we know your side of the argument. We have been through it now for a considerable period of time.

What we are offering—Mr. Jones is offering in his way and I in mine—is a possible compromise. We are not wedded to this legislation. If you have some compromise that makes some sense and is acceptable to both sides, which means both sides will dislike it, offer it. Or if you are going to take the intractable position of saying, "Oh, well, let the rulemaking go ahead; we are going to fight it down to the wire."; well, that is another matter. If that be your position, state it, so we will know exactly where you stand.

I would like to take a position where nobody is unduly hurt. That is the only intention that we have in mind. We are not pro the Berger Group and his people nor are we pro yours. We know the situation. There is merit on both sides. I think there is more merit on your side. OK?

However, that is not the way it is coming. You see what is coming. You saw what was coming a long time ago. I saw it.

Mr. GOLDSTEIN. Mr. Chairman, I appreciate your remarks and I certainly appreciate your efforts on our behalf over the years. I would like to make a few points on the question of compromise at this point, and maybe have a chance to answer some questions that have been raised by parties that are now absent.

We cannot be expected to compromise with our existence. That is the bare minimum. If the rule produces certain results and a compromise produces roughly the same results, then there is really no compromise; there is no room for compromise.

I will say this: early on this year we did present a compromise that would have extended somewhat, maybe significantly, the use of subsidized tankers if there were, indeed, a need. That idea was presented to the proponents of the rule. It was presented to the Senate Commerce Committee. We were virtually thrown bodily out of the room at that time.

I will say it resembles somewhat the position of Sohio when they expressed the desire for more extensive use of the big ships in Alaska, if there were a need. It coincides somewhat with the views of Mr. Jones as well.

There are significant differences, however, between the compromise we have presented and that of Mr. Jones. We are certainly prepared to talk about the differences, discuss them.

I will say this: despite the statements made by the proponents that they are eager to compromise, eager to present ideas, we have never received one. We have been——

Mr. BIAGGI. Have you offered them one? Have you offered them suggestions?

Mr. GOLDSTEIN. Yes. It was public—yes, they got the text of our——

Mr. BIAGGI. I just want that for the record, because you were here when they were testifying, and they said to the contrary.

That's OK. People say many things when they are testifying. [Laughter.]

I have learned that everyone doesn't tell the truth. They may tell it as they see it.

Mr. GOLDSTEIN. I will say this: our compromise—you may agree or disagree with it—it is the only compromise presented by an opponent or a proponent of the rule in 3 years. It was presented publicly. It was on the record. We made a speech about it. We prepared testimony. No one else has done that.

Mr. BIAGGI. OK.

Mr. GOLDSTEIN. I would like to just say a few words, if I may, about the rule published by the DOT, because this is new information and I think you should be aware of the statement of the DOT, and the certain inadequacies in their statement.

We have heard that between $800 million and $3.2 billion in transport savings would be made over the next 10 years as a result of payback. I went through this analysis very carefully. It was not easy. It was very involved, very complicated.

There are a number of factors that create these numbers. I will list a few of them: current charter rates per DOT, their view of what the charter rates are; their view of what the break-even rates are; their assessment of what each ship's fuel consumption is; the volume of production; the disposition of the production.

The DOT has a perfect score. Every assumption is wrong—not by a little, but by a substantial margin. I will give you one example.

I will borrow a ship from my friend Mike Klebanoff, the OMI *Columbia.* It is a 135,000-deadweight-ton diesel tanker. It is very efficient. In that size category DOT has said that the break-even rate for that ship is $4.42 per month per deadweight ton. Now for Mr. Klebanoff's ship, that gives him the ability to pay his operating costs and to contribute $1 million a year toward the capital charges on that quite expensive vessel. That vessel needs $10 million a year to break even, not $1 million.

I won't say the rest of it is any better.

Mr. Chairman, the emperor has no clothes.

We have heard today from one of the proponents that the idea of windfall profits is ridiculous. That statement is ridiculous. By definition, there has to be a windfall profit either to the owner of the vessel or the party that is chartering the vessel in the case of vessels that have long-term charters in the foreign trade.

Since all of these ships are obsolete, economically obsolete, since they are all steam powered, there is a burden exacted on the charterer every day that is not necessary. The ability to get out from under those charters is worth a lot of money. If the charters are 1 year, then the windfall would be small. If it is 10 years, the money adds up, multiplies.

Charter buyouts are common practice in the shipping business. In today's depressed market, they happen regularly. My company, for example, just this year negotiated a charter cancellation with a company that happens to be the same charterer of three of the Panamax tankers. That charter cancellation was just concluded this year.

Basically, it called for the payment of the full charter hire for the remaining life of the charter less any operating expenses that would not be incurred by us, discounted at a certain interest rate. It is routine. To say it is not a possibility is wrong.

It is also suggested somehow that these more efficient ships would simply bring the rates down a bit; that we are earning too much money; the rates are much too high, and all the modern ships somehow would remain employed. How can that be? The market is overtonnaged today. It has been overtonnaged for 3 years. If you add 2 million tons of new capacity, 2 million tons has to come out. It is not a question of taking a somewhat lower rate. It is a question of survival.

We also heard that the Panamax vessels need $11 to $11.50 to break even. This suggests, if the rates are going to come down and these ships are going to come in, the rate must be much higher than that; right?

The facts are the rates for every ship of that size have been, and continue to be, below $11.

Mr. Biaggi. They do a lot of business.

Mr. Goldstein. They do.

Finally, Mr. Chairman, I have heard a comment and I will anticipate a question about my particular company that suggests that our American profits are subsidizing the construction of foreign ships. The same parties that make that statement not too many years ago claimed that our foreign ships were subsidizing our American fleet. Now it all depends on the issue.

Mr. Biaggi. Which one was true——

Mr. Goldstein. Neither was true.

Mr. Biaggi. As the old saying goes, were they lying then or now or both times? I don't know.

Mr. Goldstein. It seems to be a handy argument. The other side is getting subsidy. We are subsidizing ourselves. Chevrolet is subsidizing Buick. That's ridiculous. I will leave it at that, Mr. Chairman.

Mr. Biaggi. Mr. Gallo.

[Statement of Mr. Gallo follows:]

STATEMENT OF FRANCIS X. GALLO, VICE PRESIDENT, VICTORY CARRIERS, INC.

I appear today in behalf of Victory Carriers, Inc. ("Victory") to give our view of CDS payback, as promulgated by the Department of Transportation and as provided in the draft bills accompanying the invitation to testify.

Victory owns and operates three vessels:

Name (DWT):	*Built/retrofitted*
Mount Washington (49,395)	1963/1981
Mount Vernon Victory (49,430)	1961/1982
Montpelier Victory (50,136)	1962/1982

Victory built these vessels at a cost of $42.8 million, without the benefit of government subsidy. We paid full dollar for these American-built ships. In 1981/82, we invested approximately another $30 million to overhaul and modernize these vessels and bring them into compliance with the Port and Tanker Safety Act requirements. We are about to spend another $6 million repairing two of the vessels to meet charter requirements. Our ships may be 22-24 years old, but they have been modernized, they are in full compliance with all applicable statutory and regulatory requirements and they meet the high standards of oil company charterers. A vessel's utility does not necessarily disappear with age, as the battleship *New Jersey* amply demonstrates.

We invested these large sums in our vessels, to the benefit we may add of U.S. shipyards, U.S. ship support industries and U.S. labor, relying on the protection of the Jones Act against foreign competition and relying on the protection of Section 506 of the Merchant Marine Act against competition from subsidized U.S. vessels.

Having acted in reliance on this statutory scheme, indeed in the very way which the statutory scheme was intended to induce, we believe it is manifestly unfair to change the rules and allow the CDS-built vessels to flood the domestic markets.

We opposed the Department of Transportation's proposed CDS payback rule and we oppose the final rule issued May 3, 1985. We believe that in allowing the wholesale diversion of the CDS fleet into the domestic trades, the Secretary has exceeded her authority. By her sweeping action she has usurped the authority of the Congress.

We believe the CDS payback will have a very harmful effect on the unsubsidized fleet. The Secretary predicted that 13 small tankers will be rendered permanently unemployed. In making this calculation she assumed that smaller CDS vessels would not seek to repay. In a lawsuit filed May 15, the Berger Group and Moore McCormack Transport stated that they intended to repay CDS on 4 small vessels. These vessels will be particularly harmful to us and it is something which the Secretary never considered. We believe that the effect of the DOT rule will be worse for the unsubsidized fleet than the Secretary projected.

In addition to the unsubsidized operators, the losers will be 800 plus American seamen whose jobs will be wiped out, the ship repairers and their workers, the ship support industries and national security. The Congressional policy of promoting U.S.-flag participation in the foreign trade is another casualty of the DOT rule. Some of the vessels which DOT would be allowing into the domestic trade have charters in the foreign trade. DOT offers no justification for undercutting the fulfillment of Congressional policy.

The CDS owners made a calculated decision to accept government subsidy and to commit to the foreign trade. If that was a bad judgment, it is neither fair nor good policy to make the domestic fleet, who accepted no subsidy, pay the price.

We welcome and will consider any possible legislative solution to the CDS payback issue. In this spirit, we have carefully considered the two draft bills which accompanied the invitation to testify. We wish to alert the Committee to a number of what we believe are drawbacks or weaknesses of these bills. We attach copies of these bills with our labels "A" and "B".

DRAFT BILL A

Our concerns regarding this bill are:

A. This bill would not ensure capital cost parity, i.e. it would allow CDS repaid vessels to retain some benefit of subsidy because:

1. it requires repayment of only one-half of the unamortized subsidy, lowering the capital cost of entering the domestic trade;
2. it does not prohibit the use of a note, ODS buyout or Title XI financing or other devices by which the capital burden of repaying CDS can be reduced or deferred;
3. it does not require continuously compounded interest; and
4. it does not by its terms require the repayment prior to entrance in the domestic trade.

B. The admission of CDS vessels is not based on a need for them in the domestic trade;

C. It allows repayment for CDS vessels which are in fact employed or have employment opportunities in the foreign trades;

D. By not requiring complete cancellation of ODS it allows ODS operators to move back and forth between the foreign and domestic trades, skimming the cream; and,

E. The authority of the Secretary, if necessary to promote competition or to avoid over-capacity, to designate the years during which the vessel may operate in the domestic trade does not protect the unsubsidized ships because:

1. there is no provision for unsubsidized vessel participation in the decision;
2. the designation must be made within 60 days of the repayment yet will cover conditions years away; and
3. there is no standard by which unsubsidized vessels, particularly smaller vessels, are assured protection. The Secretary has already decided that to promote competition all CDS tankers may repay and enter the domestic trades now.

DRAFT BILL B

A legislative solution along the lines of this draft bill could afford unsubsidized vessels greater protection than draft bill A. However, we believe the bill's standards and terms would have to be tightened. We are concerned about the following points:

1. by allowing payback in 6 month increments for the first 3 years, the bill would reduce the capital burden of entering the domestic trade;
2. the Secretary's finding justifying the initial admission of the CDS vessel may effectively bar a later protest;
3. it is not clear that a "suitable vessel" standard will not be used in the initial admission decision or in ruling on the notices of harm to bar participation by small vessels against large vessels;
4. a vessel laid-up at the time of enactment may not be eligible to protest because it is not at the time of enactment "engaged in the coastwise trade";
5. vessels beyond the end of their economic life may not protest. How rebuilt and/or retrofitted ships are to be treated is not clear;
6. the standard of inability to compete is vague. While, literally speaking, a vessel may always be able to compete, it may not be able to secure employment;
7. linking the inability to compete to the admission of a particular CDS vessel may require a virtually impossible burden of proof, especially considering the indirect nature of the bumping process;

8. the Secretary could delay ruling on the protest, meanwhile the CDS vessel is in the trade; and

9. the bill does not identify the period for which interest is payable nor does it provide that the interest is continuously compounded.

While we are critical of these draft bills, we wish to assure the subcommittee that we welcome these efforts at finding a legislative solution. We pledge our cooperation and good faith in working with the Congress and other interested parties to find a legislative resolution of this fundamental and critical issue of maritime policy.

STATEMENT OF FRANCIS X. GALLO, VICE PRESIDENT, VICTORY CARRIERS

Mr. GALLO. I would like to thank you, Mr. Chairman, for the invitation to appear here today and testify on behalf of my company and, more importantly, on behalf of the people we employ who depend on their company for their livelihood.

As you know, Victory Carriers is a small company. We own three tankers. They are all 22 to 24 years old, fully retrofitted in accordance with the U.S. Port and Tanker Safety Act.

I have sat here today and I have in the past month, 2 months, and 3 months read a lot of literature referring to things like economic life, rust buckets, et cetera. Yet, on March 4 of this year Sohio chartered two of our vessels on long-term period charter after extensive inspection and examination, after extensive checks on the domestic market as to competitive position. I don't think to refer to old vessels is necessarily akin to referring to them as rust buckets.

Mr. BIAGGI. I happen to agree with you on that score. I think that is an abused term. It might have been applicable 10 years ago. I don't think it is applicable in this.

Mr. GALLO. Thank you very much.

These charters have a provision where they can be terminated under certain circumstances. These circumstances could be triggered by CDS payback in the sense that shoppers, people who are speculating on the market, people who will try to combine a charter possibility to the detriment of someone else with a financial possibility, could conceivably, if the finances are structured properly, come in and cause a situation where these charters might be terminated.

We feel very concerned about that. Within the next week I will sign a repair contract which requires an additional $6 million in private investment, our money, unfinanced money, which will support 100 workers in the U.S. Gulf for 4 months. These charters will employ 150 Americans in the office and onboard. I assess the economic impact——

Mr. BIAGGI. Mr. Gallo——

Mr. GALLO. Yes?

Mr. BIAGGI. I will tell you the same thing I told the other witnesses this morning. We know it. We know all the things you are saying, and I appreciate it. You are a small company. It would probably be devastating. I am mindful.

That is why we took our original position. Our original position was to oppose the rule. We have effected delays. But now we are looking at a rule that goes into effect in 2 weeks. We are trying to do something legislatively.

Really, the decision you have to make collectively is you either want to compromise, if we can effect one—I don't even know if we can effect one but we are trying—or be intractable and go down fighting. That is the decision. It comes to that.

I think it is unfortunate we come to this point, but that is what we are looking at.

I know all the human aspects of it. I know the other side of it. I am not especially enthused about what they are doing. I think they had the good years and would like to come on and pick up another piece of business. That is all transparent. But they apparently have the ear and support of the administration. That was evident from the beginning. That is what we are looking at.

You can make the arguments all day. I have heard them. We have heard them. I am not sure that it will be as dismal as you say, but I agree, it will have a substantial impact. We are trying to minimize that impact. That's exactly what we are trying to do.

You can make the arguments all you want, and I would agree with you, but the only way we can deal with the rule is by going to legislation, if we can come up with something that can enable us to muster some support. If we don't have any support, well, it was a wonderful day and we had a nice hearing. We learned a little bit more about the problem.

Mr. GALLO. Mr. Chairman, I would not oppose an effort by this committee to discuss a legislative solution. This is where it belongs. I oppose very vehemently the rule, because I don't think the Executive, in my opinion, has the right to make law. The law should be made here in the House of the people. I support an effort.

I think perhaps that H.R. 2550 may provide a vehicle where both proponents and opponents of the rule can sit down and discuss what should be done to restructure the merchant marine. This is what we are talking about.

To do this by Executive fiat, in my opinion, has to be opposed.

Mr. BIAGGI. Then what you are really talking about is in Mr. Klausner's area. You are going to go to court and sue and find out whether the Executive has the ability to do it. We are trying to do it more quickly through this method. I am not so sure we will be successful.

Mr. GALLO. I would hope that somehow it would be possible to postpone the implementation of the June 6 effective date of this rule while the committee establishes a purposeful schedule of hearings. I don't mean a schedule which is vague. I mean dates and times where the people can come and we can work out a bill that would be satisfactory to all concerned.

The problem now is we have a window, a window that in my opinion should be closed until the Congress has the opportunity to restructure the law as it sees fit.

Mr. BIAGGI. Yes, I understand that, Mr. Gallo. The fact is, even if we go the legislative route, it will take some time. If you give the proponents of this bill 30 days, they will be in there with a whole bucketful. The question is, How can we do it legislatively?

That is why we have encouraged meetings. That is why we have tried to get people to compromise. Apparently, it has not been productive. That is why we are having these hearings. It has not been productive.

I don't think we should have to go through it because we know exactly where we are. The way I see it, if we cannot do it legislatively, you are going to fight it in court and question the Executive's ability and right to do this. What the outcome will be only God knows, but you will be fighting to the bitter end. If you lose, all the dire things you said will happen may or may not happen. I think it is unfortunate.

Mr. Schmidt.

[Statement of Mr. Schmidt follows:]

STATEMENT OF SANFORD V. SCHMIDT, MANAGER, CHARTERING AND INDUSTRIAL RELATIONS, AMERICAN TRADING TRANSPORTATION COMPANY, INC.

Mr. Chairman, ladies and gentlemen of the Subcommittee: Thank you for this opportunity to appear before you to present our views on the recent proposals to permit vessels built with federal subsidies to enter the domestic trades in direct competition with vessels which have not had federal construction or operating subsidies. This issue is absolutely critical to the future of the remaining unsubsidized U.S. Flag fleet and my company absolutely opposes the entry of these ships in the domestic trade.

My name is Sanford V. Schmidt. I am Manager of Chartering for American Trading Transportation Company, Inc. In this capacity I am directly responsible for the chartering of our vessels and I am intimately familiar with the difficulties facing our tanker fleet today.

For those of you who are unfamiliar with our Company, American Trading is the owner or operator of eight U.S. Flag tankers ranging in size from 27,500–57,884 DWT. Our New York based Company has been engaged in the ocean-going transportation of liquid and dry bulk cargoes for more than forty-five years. All of our vessels were built in the United States without construction subsidy and all are operated without operating subsidy. We own three new 50,000 DWT tankers, all delivered in 1982 and 1983, capable of carrying a full range of cargoes from crude to militarily essential jet fuel.

Let me tell you of a recent investment decision that we made and the history behind this decision.

About one year after the Port and Tanker Safety Act become law in 1978, we analyzed our fleet and the manner in which we had acquired ships in the past. It became clear to us that the U.S. Flag domestic fleet was aging and many vessels could not be refitted to comply with the requirements of the Port and Tanker Safety Act. It was also clear that technology had progressed and new ships could be built and operated with greater efficiency. Finally, it was also clear that there was a need for tonnage to move of Alaskan Crude Oil to consuming markets. At the same time, we analyzed the potential market for trading foreign flag vessels and for the trading of U.S. Flag vessels built with subsidy. We knew that the latter ships, in accordance with law, would be required to trade in the foreign commerce of the United States and that they would not be permitted to trade in domestic commerce.

Thus, with full knowledge of the markets, reliance on the provisions of the Port and Tanker Safety Act, the demand for the transportation of Alaskan Oil, and the law which requires that these ships built with CDS not be entitled to enter the domestic trades, we began discussions with U.S. shipbuilders in an effort to modernize our fleet. Our objectives were to enter into a contract for the construction of tankers which would offer economies of scale in construction and economies in operation, meet the new stringent U.S. pollution and safety requirements, be flexible enough to permit us to handle a wide range of petroleum products—from jet fuel for the military—to heating oil for utilities, and also handle crude oil.

We contracted with National Steel and Shipbuilding in California for the construction of up to six crude and product tankers slightly in excess of 50,000 long tons deadweight each. These ships were the most efficient available in terms of fuel consumption as they were fitted with modern slow speed diesels, they were fitted with double bottoms, collision avoidance systems, crude oil washing systems, inert gas systems and a host of other features designed to increase safety and reduce the possibility of pollution. Our new tankers cost approximately $75 million each.

As you are aware, the Maritime Administration has pursuant to Section 506 been regularly permitting ships built with construction subsidy to enter the Alaskan trade on a six month basis. When we began to take delivery of our ships and pointed out to the Maritime Administration that our vessels were fully qualified to transport Alaskan Oil, we were told that under Maritime Administration rules, we did not even have the right to be heard in our protest against these subsidized ships taking a trade for which we were fully qualified under the law. In spite of all this, our ships have been in the Alaskan Trade carrying crude oil from Alaska to the West Coast and Gulf Coast and from Panama to the Gulf Coast and East Coast because of our efficiencies.

In 1983, the Department of Transportation put forth a proposed rulemaking that would allow tankers built with Construction Differential Subsidy to payback that subsidy on some basis or another and enter the domestic trades because of an apparent need for these ships. Accordingly, we reduced our acquisition plans to three vessels. However, in 1984, the Department decided that subsidy built ships were not required in the trade. Thus, during 1984, we managed to keep two vessels employed for virtually the entire year in the Alaskan Oil trade. Others participated in the trade and there was no shortage of fully qualified ships. The minute the subsidy built ships were allowed back in the trade, we lost the business on our private tankers. Our experience and that of other owners in 1984 proves, from a factual standpoint, that subsidy built ships are not needed in the Alaskan trade.

After dealing with the Maritime Administration and their waivers, and the Department of Transportation's wholesale payback proposal, which will turn the Merchant Marine Act on its head, we are now faced with a proposal from the legislative branch to grant domestic trading rights to some subsidy built tankers.

Why is there any impetus on the part of the Department of Transportation and the Congress, to upset what was and is, a carefully planned and effective system to protect private investment? We have been told that there is demand—yet the trade operated for a full year without subsidized ships and can certainly continue to do so. We are told that non-subsidized ships are old—yet our ships of which I am speaking are only two years of age, while the subsidized VLCCs are 9.5 years of age—only two years away from the actual average age of all VLCCs scrapped last year. We are told that there will be a federal fiscal benefit from the proposals—yet we know better for the ships which are recognized to be in jeopardy are those whose debt has been guaranteed by the Federal Government. Frankly, we feel that the Federal Government in a democratic society should not put its commercial interests above that of private capital. We are told that the subsidy built ships are more efficient—yet their fuel consumption alone is over 100 percent in excess of the truly modern VLCC's under construction. We are told that they are really needed for Alaska—yet this is not the case and if it were, and if small steam ships are not suited to this trade, why are the ships of 35,000 and 80,000 GWT tons being considered for repayment? We are told that our militarily useful ships are not needed in the U.S. fleet—yet the Navy and Department of Defense have disagreed.

The analysis completed by the Department of Transportation states that the outlook for our militarily useful tankers is bleak and that the fleet size will decrease regardless of their rules. We agree. DOT likewise recognizes that our Alaskan Oil market will decrease to 20 percent of its former volume should subsidized ships enter the trade. DOT states that there will be a loss of 800 jobs by allowing subsidized ships into the domestic trades. Given all the recognized negative impacts from its own proposed rule, we would like to request that the Department, which has responsibility for promoting the U.S. merchant marine, "promote" some other industry which can afford devastation.

We are opposed to this legislation and indeed to the position of the Department of Transportation and the havoc that it has, and continues to wreak upon our company. However, we would like to point out what we believe to be a number of flaws in the proposed legislation, some of which may have been addressed by various other legislative proposals which have been discussed or put forth.

1. The source of the funds to payback CDS should be restricted and Title XI guarantees should not be permitted for then the Government's balance sheet will be unaltered. Cash payment should be required. Debt instruments of dubious worth should never be accepted again by the Government. At a time when the Title XI fund is nearly insolvent, it is illogical to permit the use of Title XI for such a speculative investment.

2. Since the real impetus for the rule appears to be the desire of the legislators in the DOT (and the use of that term is no accident) to have large ships in the Alaska Trade, why not restrict the entry to ships above 200,000 DWT and also restrict the trade to Alaska and Panama?

3. Some ships are gainfully employed or have been recently acquired with full knowledge of their trading restrictions. Why not exclude these ships by statute from the trade?

4. The owners of subsidized ships should not be afforded the option of paying back CDS alternatively obtaining waivers under Section 506. Waivers should be prohibited if payback is enacted in any form.

5. The Government should insist on compounded interest on any CDS that has not been repaid to date, for most competitive owners do have trouble in obtaining interest free loans.

6. Any legislation should state clearly that the DOT Final Rule was void so that there would be only one procedure for the payback of CDS.

We would urge that those considering legislating on this subject carefully and clearly state their intentions and not permit the Department of Transportation and the Maritime Administration to turn laws around 180 degrees to suit favored interests as they are now proposing.

It is American Trading's belief that it should be the Congress' objective to pass legislation which will on balance be the best for the country overall, not best for oil companies, or for foreign oil companies with long-term VLCC charters, or for owners of subsidized vessels with ships already on long term profitable charters, or for already bankrupt shipping companies. We believe that, when viewed in this light, it is clear that on the whole it is better for this country to maintain its maritime base and encourage its growth by ensuring the vitality of the domestic fleet than it is to permit CDS payback and further accelerate the decline of the true domestic fleet.

Coincidentally, ladies and gentlemen of the subcommittee, yesterday was National Maritime Day. In its message to us, the Military Sealift Command said, "It is clear that our national defense and economic security have been and will continue to be dependent in large measure on the ships and personnel of the maritime industry." We urge you to consider this point carefully in your further evaluations of this legislation.

Thank you.

STATEMENT OF SANFORD V. SCHMIDT, MANAGER, CHARTERING AND INDUSTRY RELATIONS, AMERICAN TRADING TRANSPORTATION CO., INC., NEW YORK, NY

Mr. **Schmidt**. Mr. Chairman, ladies and gentlemen of the subcommittee, thank you for the opportunity to appear before you to present our views.

In contrast to Mr. Gallo who has older vessels, our company has brandnew vessels. We built our vessels in 1982 and 1983. I won't go through the arguments. You say you know the arguments.

We invested private capital, $225 million. You have heard it all. There is no reason to bring it up again; as you say, you have heard it over and over again.

The problem that we have is you are asking us to compromise when we are in the middle of the lake drowning and we have nowhere to go. You say compromise, compromise, but we cannot compromise——

Mr. **Biaggi**. Just a minute. We have been asking you to compromise for months. Now someone in the previous group has said, it takes two to do that. Well, sometimes compromising isn't possible. This may be one of those times; I don't know. That would be a rare occasion. I always think there is an opportunity for compromise in one form or another. If you want to remain intractable and not participate in it, or to the point where you are spelling out your own demise, well, I wouldn't recommend that you sign your own death warrant.

Do you see what's happening? One year when the fortunes look good for you, you take a firm position. Now they look good for the other side, and they take a firm position. We should have done this months ago.

I am not asking you to compromise. If you don't want to, don't. We are trying to effect a compromise that won't hurt anybody too much. If you want to take your hard position, be my guest.

Mr. Schmidt. Chairman Biaggi, the problem——

Mr. Biaggi. I am more concerned about the industry than any particular concern of individuals of your company, an individual company. That is my concern.

Mr. Schmidt. Certainly, American Trading does not dispute that. What we do dispute, though, is whether or not payback is beneficial to the industry as a whole. That has been our dispute all along. The fact that our company happens to suffer enormously——

Mr. Biaggi. I have agreed with you. I have always been against it. We are on the record as being against it. We are looking at something else. We are looking at something real—the rule is in place. It is going to be in place. It is going to be effective.

Mr. Schmidt. I absolutely agree——

Mr. Biaggi. That is why we are trying to do this. We are trying to muster a body of support. If we don't muster it, then so be it.

Mr. Schmidt. But right now the problem is legislation. I grant you that, if there was a compromise that was a better position than the final rule, that has some attraction to us. Certainly the legislation as it has been proposed does not protect us anymore. It is still a wholesale admission of CDS tonnages——

Mr. Biaggi. I told you we are not wedded to the legislation. Correct it so that it would be acceptable to you. Make some suggestions. Do I hear any besides what Mr. Goldstein stated, which is totally unacceptable to the other group?

Apparently, Mr. Klebanoff or maybe some other witness will have it.

Make it. It is a wide-open forum.

Mr. Schmidt. Well, the reason it is unacceptable to the other group, though, is because it is a retraction from what has been handed to them already. They want everything, and we have everything to lose and nothing to gain.

We are certainly willing to compromise if there is some way that we can compromise and hold our position.

Mr. Biaggi. If you can come up with some kind of a compromise—I spoke to Neal Smith, of the Appropriations Committee, and if we could come up with a compromise, he would probably do something with that amendment that was passed. But we need a compromise, something that will be supported.

We just offered these two vehicles. If you don't like them, what do you like? What do you like that could be reasonably expected? Right now this language, if it gets on the Senate side, is going to be killed by Senator Stevens. You know that.

Mr. Schmidt. I can make some points. I would like to make some points.

Mr. Biaggi. Make some points that help us. Don't make those points that make your position. We know your position. We are trying to help you.

Mr. Schmidt. Some of the infirmities of this legislation that we see in the very brief time we had to review it, Congressman, are:

No. 1, we believe that title XI should not be used. Now that may not have any impact on CDS the way it is sounding from the panels here, because everybody but Seatrain does not need it. Maybe title XI is not a major issue. We personally believe that title XI is a vehicle right now that should not be used.

Mr. **Biaggi**. You say that, and then we have Seatrain testify that, if they don't get it, they are in trouble, serious trouble. Do you see what I mean?

Mr. **Schmidt**. Absolutely; because everyone looks at their own personal view. But if you take——

Mr. **Biaggi**. I am not looking from a personal view. I am trying to help as many as we can. I am trying to help the industry.

OK. I will accept your suggestion. We will consider it.

Mr. **Schmidt**. My feeling on title XI is, when you have a fund that is potentially in default, you ought not to be putting more risk into that fund; that's all.

Mr. **Biaggi**. That is a point of view. That is a valid point of view. There are people who have——

Mr. **Schmidt**. Another point that we would like to make is——

Mr. **Biaggi** [continuing]. Other thoughts.

Mr. **Schmidt** [continuing]. That the legislation as drafted would potentially allow all vessels, all CDS vessels, to pay back. Yet, if you listened carefully, as we did, to DOT's presentation, not only do they presuppose that none of the small vessels will come in, but they only talk about VLCC's. Why aren't we limiting it to just VLCC's over 200,000 tons? Let's focus on what we are trying to do. If these vessels are so efficient, then let's make those the only vessels that get in.

Another infirmity that we felt should be mentioned is that there are some vessels—again, these are vessels below 200,000 tons—that are gainfully employed. Why are we giving the right to those vessels to have an option? "Come into our trade if you like it better or stay where you are." We don't think that is appropriate.

Another point we felt should be made was that waivers—it is not clear from the legislation whether or not the vehicle of a section 506 waiver would still be available notwithstanding the payback scheme. I think it should be clear that we are going to go one way or the other, not having a wide open free-for-all: "Take whatever you like best."

Again, we are giving up everything.

Mr. **Biaggi**. I know what you are giving up. So far you have made a number of suggestions that I have never heard before, and I think there is some substance to them.

Mr. **Schmidt**. Another point which we felt in reviewing this legislation was that it is not clear whether or not compounded interest is paid as opposed to regular interest or any interest, and whether or not the vehicle of the payback is via notes or is by cash.

It is extremely unfair, we think, to the American flag owners such as ourselves who don't get interest-free loans, who don't get loans without compounded interest, to have someone else come into our trade and be able to pay back without having been forced to pay compounded interest.

Another point that I believe is not properly stated in the legislation is, Who has the standing to oppose the entry of the CDS vessels into the trade? As you know from the history of the section 506 waivers, American Trading has struggled vociferously and tremendously to point out to the Maritime Administration that our 50,000 tonners can operate in the Alaskan trade and have. We had 80,000 tons of vessels, two vessels in that trade, and I can tell you, Congressman, I am the chartering manager for American Trading. Those two vessels right now, one of them has no employment as of today; the other one has employment until June 1. I have nothing after that for that vessel, a brandnew 50,000 tonner.

It should be clear in the legislation who has standing to oppose. If it is everybody, then it should be stated that it is everybody, so that we don't get an end run by the other side. You know, as you say, there is going to be court litigation and court fights, hearings. The Maritime Administration or the DOT does not say, "Oh, anybody who is under 100,000," or whatever the number is, "doesn't have standing."

We think that the standards for the finding of the need, the statute uses the term "necessary"—and what is the other one?—"necessary and appropriate" to carry out the purpose of the act. That is a standard that is set for the first hearing in determination by the Secretary of need. What is going to happen for the second hearing, though, in the next 6 months? I can assure you that American Trading is going to be in there fighting because I can tell you there is no way we can stand to have more vessels in the trade. We cannot stand what we have right now.

Mr. **Biaggi**. I think I raised that point with the Assistant Secretary when he was here. What guarantee do you have that they won't continue and extend it?

Mr. **Schmidt**. Absolutely. There is no question about that. That is another infirmity.

We don't have any guarantee other than his word here today that they won't reopen the window. There is no question about that, too.

The finding of need in the second hearing, though, seems to shift the burden to us, American Trading, or to those who would object to this legislation or to the entry of the CDS vessels, to our showing that we cannot compete. What in the world does that mean? "Compete" is an untested legislative word right now in the context of the marine industry. I don't know what it means.

I can tell you that right now the cashflow for American Trading on every voyage that I do, a typical 14-day voyage, is a half a million dollars—excuse me—yes, a half a million dollars negative cashflow to our company. That is money that is disappearing. It is gone.

Mr. Mills talks about breaking even. I will tell you I would love to break even. I would be the hero in my company if I could break even.

Mr. **Biaggi**. You just confirmed what I have been saying. I understand where Mr. Mills is coming from.

Mr. **Schmidt**. Basically, Mr. Chairman, really that is the extent of my comments——

Mr. **Biaggi**. Do we have your statement, Mr. Schmidt?

Mr. **Schmidt**. You have my statement. It has been submitted.

Mr. **Biaggi**. I want to thank you.

If my memory serves me correctly, you made the most significant contributions to some possible points to pursue of any panel so far. I appreciate it.

We will now have a recess.

[Recess taken.]

Mr. BIAGGI. The meeting is called to order.

Mr. Klebanoff.

[Statement of Mr. Klebanoff follows:]

STATEMENT OF MICHAEL KLEBANOFF, PRESIDENT, AMERICAN MARITIME ASSOCIATION

The action of the Secretary of Transportation in issuing the rule that has so long hung over the head of coastwise shipping is a catastrophe. Not merely the effect but the announced purpose of this action is in that order of magnitude.

Although the law promised owners like the members of the American Maritime Association that subsidized tonnage would operate exclusively in foreign trade, and $4.5 billion has been invested in coastwise tankers during the last ten years in response to business estimates of straight domestic demand, permission has now been given for four million tons of subsidized tankers to invade our trade that at full stretch uses about six million tons and that has lately been going through an economic wringer.

What does the Secretary tell us will be the consequence? Her statement predicts that rates will fall at least to the break-even level of efficient tonnage, which she defines as operating costs plus debt service—that is, no profit. This she regards as a substantial benefit to shippers, and her order purports to measure this benefit more or less exactly. It adds that of course rates may really fall to lay-up levels, which would be an even greater benefit, but that to be conservative, the break-even level provides sufficient "benefits". A 10-year forecast of "savings" is made on that basis, and a very inadequate forecast of the amount of shipping that will be forced out of business.

The Secretary expects these results; she considers them beneficial; she therefore deliberately intends to bring them about by issuing the order that will cause them. Is this what Congress intended when it legislated to develop and maintain the merchant marine?

Had I as a shipowner expected the government to adopt a non-profit policy and to enforce it by deliberately smashing the long-standing statutory markers, my company would not have invested upwards of $400 million in American shipping during the last ten years. You may rely on it that the coast-wise industry as a whole would not have invested $4.5 billion in new tankers—not a penny of it government money.

I say with all consideration that this action is a historic breach of faith. If there had been a runaway freight market because of huge demand and insufficient tonnage, it would still have been desirable to maintain the statutory framework and to let the market itself breed the necessary expansion of tonnage at its own expense; after all, that is what happened when Alaska opened up. A safety valve was even available; we went along with the Maritime Administrator in 1978 when he began to give temporary waivers to subsidized ships under existing law while the coastwise fleet was building.

But now there is no boom; there is a depression. I mentioned the figures when I last gave testimony here: nearly two million tons lost from the tanker fleet since 1982, and one million tons laid up, with rates already at break-even or worse for better tonnage. Into this saturated market the Secretary has now poured an additional four million tons of all shapes and sizes. This is a profound error of judgment, made in a spirit and with a purpose flatly opposite to what we have understood to be the policy of the shipping laws: to promote, not to destroy, a commercial merchant marine.

We look therefore to Congress to rectify this wrongful act.

Our members have not had time to study in detail proposals that lie before the Committee, and will give their comments to your staff as soon as possible. In general, the basic legislative principle that should be established in contemplating subsidized entry is need for service and adequacy of existing service. That principle is inherent in the whole Merchant Marine Act: it is in the basic statement of policy and in various individual sections. The Secretary's order entirely ignores this formal Congressional policy.

STATEMENT OF MICHAEL KLEBANOFF, PRESIDENT, AMERICAN MARITIME ASSOCIATION, ACCOMPANIED BY JOSEPH A. KLAUSNER, COUNSEL

Mr. KLEBANOFF. Thank you, Mr. Chairman.

First of all, I would like to thank you for the opportunity once again to testify before your committee.

I would like my written statement to be placed in the record. In order to save time——

Mr. BIAGGI. Without objection.

Mr. KLEBANOFF [continuing]. I will not repeat some of the points already made by my colleagues here in front of you. I do have a few points to make basically about compromise, because that is what you really want to hear.

I think you agree with us that our ships will be displaced to the extent that CDS ships come in. In our own company we are talking about $300 million worth of Jones Act ships that are going to be inconvenienced, to say the least.

The question comes as to how do we compromise when we have to give something and we don't get anything from the partner. The two-to-tango angle is quite clear——

Mr. BIAGGI. Accept this, Mr. Klebanoff: Right now it is their ball game.

Mr. KLEBANOFF. I understand that.

Mr. BIAGGI. That is the difference.

Mr. KLEBANOFF. In order to try to reach a compromise where we will have to give something and they give us nothing, I would like to suggest some thoughts right now that address themselves to compromise but have not been addressed themselves in the two bills that we have before us.

One way would be perhaps for us to tender to the Government those ships that are displaced by CDS ships and have them pay us our equity and our debt, most of it being title XI debt, so that we can retire gracefully, not be inconvenienced the way we will be if this is not done.

The other alternative is for you perhaps to suggest an alternative compromise, and that is that you buy out the CDS ships because they claim they have nowhere to go.

Somewhere the Government has to decide, do we go out or do they go out, because we cannot both stay in. There is not room for both. You have concurred with that, and you have heard enough testimony where everybody admits that some ships, many ships, including most recently built ships in every way more efficient than the CDS ships—if they come in, we have to go out. There is no room for both.

There is not a single barrel of oil that has not been moved because of lack of ships. It has always moved.

You have also heard that the consumer will not benefit by it, by any new ships coming in. It is just a question of who keeps the money.

Beyond that, I see no other alternatives to add to your two bills in some way language that will allow the Government to either take us out or to take them out. You have a choice.

Mr. **Biaggi**. If we have no choice, then what you are saying is we should let the status quo remain.

Mr. **Klebanoff**. Well, there are other compromises. If you want to limit it to certain large ships perhaps, at least we would know where it is all going to end.

Mr. **Biaggi**. Mr. Schmidt made some recommendations. Do you agree with some of his recommendations?

Mr. **Klebanoff**. Yes, we agree that there may be some room for compromise.

Mr. **Biaggi**. Well, we have something to work with, don't we?

Mr. **Klebanoff**. Right.

I would like Mr. Klausner to address himself to a compromise that perhaps may be acceptable to all.

Mr. **Biaggi**. Sure. Mr. Klausner.

Mr. **Klausner**. I should begin, Mr. Chairman, by remarking that our testimony on the appropriations bill was designed to give you a vehicle for the project that you have underway here. As you recall, it is subject to your further action. I thought I should perhaps say that in order to balance some observations that have been made earlier in the day.

I should also say that the testimony that I am going to lay before you is in behalf only of the American Maritime Association and does not purport to speak for other persons who are even at this table, other interests in the industry. It does not attempt to bind them in any way.

It has seemed to us that the fundamental requirement of fair legislation is that people should come in whose ships are needed in the trade; that the first criterion is whether the Jones Act fleet is failing in some material way to provide adequate service.

Now that is the fundamental of the statute itself in many sections, and it is the foundation of the present waiver provision.

Now we earlier proposed, somewhat along the lines of what I suppose I should call the Jones bill, that there should be a permission to operate consecutively instead of merely for 6 months in the year on a finding of continued need for the service.

I think that we would find acceptable the additional provision that, if at the end of the 3 years mentioned in the Jones bill a vessel had operated consecutively during that time, prima facie it is needed in the trade. Then it should, without further complication, be permitted to repay the subsidy.

What this does is that it mitigates the force of entry by this fleet, which I hope you will not regard me as being contentious if I describe as the inferior fleet. Its entry, if conditioned upon real finding of need by the maritime authority, the Secretary I presume nowadays, its entry would come in mitigated form, in absorbable form.

Now you must not overlook that if the trade should revive, you are, by allowing this form even of mitigated entry, you are diluting the possibility of new construction. I think it is fair to say that the action of Congress last year in adopting the blocking legislation had this consequence:

First of all, I think that the shippers, the oil companies, concluded that that was the end of the payback. The result was that for the first time in years, while this whole thing has been hanging

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over the heads of the industry, they were willing to give term charters and, very significant, Exxon undertook to build these two VLCC's. That kind of expansion and replacement in the industry will be to some significant degree diluted by this proposal.

Now I bound to say to you, Mr. Chairman, that although the payback addition after 3 years of consecutive operation was not in the original, our friends on the other side rejected this plan directly. They testified against it. They were quite unwilling to listen to it.

But I venture to say to you that this strikes us as being the framework for a fair disposition of the matter. It lets them in as they are needed. It lets them in consecutively. If after this stated period they have been in consecutively, then they may come in permanently.

I repeat, also, that this is a proposal or a suggestion strictly of the American Maritime Association.

Mr. **Biaggi**. Ms. Mikulski.

Ms. **Mikulski**. Thank you, Mr. Chairman.

I appreciate your leadership in trying to fashion a compromise in this legislation. I also share this panel's frustration with the change of the rules in the middle of the game, and also that the Department of Transportation has used rulemaking authority to really create a new national maritime policy.

However, given the practical realities of a rule to be implemented on June 6, I would like to go through a series of additional criteria than what you suggested, sir, to see what would be some of the components of a compromise. Rather than getting a reaction from the entire panel, I would like to address my remarks to Mr. Goldstein since he is here representing the American Institute of Merchant Shipping.

Of course, Mr. Schmidt, you represent my hometown team, so I don't want to talk like it is just that I am interested in this only because of our tonnage there, though I am.

In terms of this, Mr. Goldstein, what would you think in terms of putting a grid on this window? One would be to have a component that would limit the size of ships which would pay back CDS to those, say, above 200,000 tons.

Mr. **Goldstein**. First, let me say that, on behalf of the institute as well as my company, I would like to associate myself with the remarks of Mr. Klausner of the——

Ms. **Mikulski**. You say you would?

Mr. **Goldstein**. I would like to, yes.

Ms. **Mikulski**. Thank you.

Mr. **Goldstein**. On the issue, by the nature of the market and the attractiveness of the subsidized vessels themselves, the waiver provision naturally would only apply, as it has in the past basically, to vessels over 200,000 tons. Those are the ships that conceivably would provide some economic benefits. The other ships are in surplus. The market is awash for vessels under 100,000 tons. We have scrapped dozens of ships under 100,000 tons. The waiver procedure in a natural market way would only pertain to the biggest ships.

Ms. **Mikulski**. What about limiting the total amount of tonnage which could enter the domestic trade with CDS payback, picking up on Mr. Klausner—there is only so much room in this particular waterway?

Mr. **Goldstein.** That is true. I think if we are talking about a number of VLCC's, each one is approximately 250,000 tons on the average. At the present time there are two vessels which operate domestically under 6-month waivers under section 506. Beyond that, there would have to be some immediate damage, some ship displacement. Typically, you would achieve that by replacing not 30,000 tonners but more likely 120,000 tonners. Then there would be a subsequent displacement in other trades. So there would be significant damage. It is a very narrow market. I have to express that.

If you accumulate all of the ships that are chartered to the ANS producers, you have something like 2 million deadweight tons. The seven VLCC's alone are 1.8 million deadweight tons. We have to be very careful about permission to pay back or for the waivers themselves.

Ms. **Mikulski.** What about a compromise that would prevent the use of title XI or unsecured notes to pay back CDS?

Mr. **Goldstein.** Well——

Ms. **Mikulski.** Or notes at all?

Mr. **Goldstein.** It would have limited value. Most of the parties reject the idea of title XI. One party has stated that it requires title XI. I am not speaking for everyone here, but I think we would let that issue alone. If title XI were to be required by one party, allow that party to use it.

Ms. **Mikulski.** Last but not at all least, you will be followed by Mr. Frank Drozak, who has been very patiently waiting, who will offer a compromise to the committee in which he is going to suggest limiting each vessel owner who wants to pay back to just one ship to come into this particular trade. Would you share with us your reaction and maybe other panelists might do so, too, just for the sake of creating some discussion on it?

Mr. **Goldstein.** I think I would start by saying that we would prefer that the compromise be in the form of a waiver procedure. We appreciate that at the same time the idea has some merit in that we are reducing the number of ships and the capacity of the ships that would be potentially repaying the subsidy. We are talking about mitigating the impact. Again, it is a pretty dangerous calculation on our part. If we are wrong about the ability of the market to digest that tonnage, we are the ones who are going to be injured.

I think we would prefer the waiver procedure, but I would not want to rule out of hand the suggestions of Mr. Drozak.

Ms. **Mikulski.** Thank you very much. Unless someone has additional comments, I know we need to move on.

Mr. Goldstein, though I directed my questions at you, I would like to thank the panel because I think the hearing has also turned into a skull session in trying to come up with some legislative remedies. I thank you for your really extensive patience and your participation. I think all of you—Mr. Schmidt, Mr. Klausner, yourself, and other panelists—have really given us some benchmarks to try to fashion a compromise package. I thank you very much.

Mr. **Goldstein.** Thank you.

Mr. BIAGGI. Thank you very much, gentlemen.

Our next panel consists of Mr. Frank Drozak, president, Seafarers International Union of North America; and James F. Paterson, vice president, National Maritime Union of America.

[Statement of Mr. Drozak follows:]

STATEMENT OF FRANK DROZAK, PRESIDENT, SEAFARERS INTERNATIONAL UNION OF NORTH AMERICA, AFL-CIO

Mr. Chairman and members of the Subcommittee, my name is Frank Drozak. I am President of the Seafarers International Union of North America, AFL-CIO.

I appreciate the opportunity to testify today on the recently released Transportation Department rule that would permit for one year the unrestricted admission of vessels built with construction differential subsidy (CDS) into the domestic coastwise trade, following repayment of the subsidy.

The Seafarers International Union has always opposed the blanket repayment of construction differential subsidies. We will continue to oppose CDS repayments because of the detrimental effect they have on the domestic tanker fleet. The U.S. merchant marine serves as our nation's fourth arm of defense. The primary casualties of this rulemaking would be the small product carriers, which have the greatest military utility. We cannot afford to let them disappear. Additionally, if allowed to stand, the DOT rule would effectively throw hundreds of American seamen out of work.

DOT's rule rejects the underlying principles of Titles V and VI of the Merchant Marine Act of 1936, which promotes U.S.-flag shipping and U.S. shipbuilding capability, by encouraging the transfer of subsidy-built vessels to the domestic trade. It thereby exceeds its authority in its attempt to dismantle a congressionally-mandated program. That authority lies solely within the Legislative Branch.

This rule is contrary to the purpose of the Jones Act, which ensures the maintenance of a healthy domestic fleet by reserving domestic waterborne commerce to U.S.-built and -owned vessels, competing without the benefits of federal subsidy. Jones Act tanker operators built their vessels and made their business decisions in a subsidy-free environment. It is unreasonable to expect them to plan ahead in a continually changing regulatory environment. Now these operators are faced with a flood of unfair competition that would result from a blanket waiver of CDS restrictions.

Many unsubsidized vessels would be forced into permanent lay-up. The current enormous surplus of tankers in the coastwise and preference cargo trades would make alternative employment for many of the vessels unlikely and would devastate all segments of the tanker fleet. We believe this surplus tonnage would in turn drive rates down in all of the tanker trades, forcing many operators serving the Gulf and East Coasts out of business. It would also eliminate any residual demand for new tanker construction in our domestic shipyards. The unemployment affecting thousand of American seamen would be compounded by the additional thousands of workers in the shipyards, on the docks, and in other allied industries thrown out of work.

Existing tankers in the domestic trade are essential to our national defense because they provide critical sealift capability. The Joint Chiefs of Staff have noted that, "There is a significant shortage in the sealift required to deliver the fuel necessary to sustain deployment of U.S. forces." Further, Vice Admiral William Rowden, Commander of the Military Sealift Command, has complained that large containerships and tankers "are not as suitable for the carriage of military cargo as the break-bulkers and handy-sized tankers they have displaced." These are precisely the small, clean oil product tankers that would be forced into lay-up as a result of DOT's new rule. The department argues that such vessels would be available during a crisis from the Effective U.S. Control fleet. I would ask this committee whether it agrees that our military support during an emergency should be entrusted to a foreign-flag ship with a foreign crew of possibly mixed loyalties.

Mr. Chairman, CDS payback has been a controversial issue for many years, over which various sectors of our industry have honestly disagreed. It is for this reason that we do support some form of fair and equitable compromise where the harm to existing operators is minimized. I know that several legislative proposals are currently under consideration. Over the last several months, I have worked with SIU-contracted operators to arrive at a compromise that would be fair to all parties on every side of this issue. Although I am not wedded to any particular compromise, I might suggest an arrangement by which each shipping company is allowed to repay the construction differential subsidy on one vessel. Such exemptions would be limited to VLCCs. This union is caught between good, sound operators in a situation where everyone could get hurt. Therefore, I believe that the only equitable and fair solution to this problem is to allow one vessel from each company.

Further, we would not object to the Secretary of Transportation being granted the authority to allow additional vessels into the trade on a case-by-case basis, upon a showing of special circumstances. This authority of course could only be exercised after a full administrative review of the proposed payback and its effect on existing operators in the trade.

We note with interest several legislative proposals currently under consideration that would slow or alter the process of CDS repayment. Provisions to allow tanker operators to file a "notice of harm" with DOT because of disruptive competition from a CDS-built vessel would also serve the interest of fairness, and would give these operators some protection from the cost advantage of CDS payback. Permitting subsidized operators to engage in the domestic trades on an alternate-year basis could also form part of an industry-wide solution.

Let me emphasize that we remain open to a discussion of the various alternatives and share this committee's desire to seek a solution to the CDS payback question that is fair and equitable to all of the concerned parties. We urge the committee to take quick action, so that we can finally close the chapter on this issue and move on to the many other problems facing our industry.

Thank you.

STATEMENT OF FRANK DROZAK, PRESIDENT, SEAFARERS INTERNATIONAL UNION OF NORTH AMERICA

Mr. DROZAK. Mr. Chairman, I appreciate the opportunity to appear again before this committee.

I would like my statement to be entered into the record, and I will just try to make a couple comments.

Mr. BIAGGI. Without objection.

Mr. DROZAK. Mr. Chairman, we have had this issue before us last year. We asked for an extension at that time knowing that if some kind of a compromise was not worked out, that we would be faced with DOT promulgating the rule.

During that period of time, Mr. Chairman, I met on behalf of the SIU, with our contracted operators, to come up with some type of an understanding. I had hoped we could advance a solution that wouldn't severely harm any particular operator but, instead, would have kept all present operators we have in business.

Unfortunately, as you have witnessed today, there remains a lot of difference of opinion. I certainly believe for the best interest of this industry that we must come up with a compromise. Unfortunately the industry is in the worst shape I have ever seen—and certainly if something is not done within the next few years there won't be an industry for us to talk about. We are down to some 380 ships in the American flag, U.S. flag fleet today, a loss of some 200 ships since this administration has taken office.

I have carefully reviewed this issue because, frankly, I am in the middle. All of these operators are my friends, and they are friends of this union. We have worked very closely with them over the years to establish what they have today because it established jobs and job security for SIU members.

We will suffer as much as anyone else by a compromise because, whichever way it may go: If we lose jobs, the rule goes into effect, we lose, and if there is a compromise, we still are going to lose. However, in the event of a compromise the penalty will not be as bad as it would be, in my opinion, if the rule simply goes into effect.

My position has always been, and still is, to oppose the CDS payback. Faced with an untenable situation, I would propose, Mr. Chairman, that we allow one VLCC of each company or its subsidiaries into the domestic trade and close the window permanently and not have any windows open at all, and let that be it.

Mr. Chairman, I would support your ideas, your bill or Mr. Jones' bill, or any other bill or recommendation that might bring about a solution to this matter before it is too late.

I, too, Mr. Chairman, would work with you and your committee and our staff to make every attempt to get whatever may be agreed upon to be adopted by Chairman Neal Smith, and also on the Senate side, to see if we can get something implemented right away before it is too late.

I realize that it is going to be damaging to each one of the operators in the domestic trade. It will certainly help some of the operators that have ships that were built by CDS, for which we have lost our international market.

I point this out, Mr. Chairman, because of what has happened. We are now shipping overseas 500,000 to 600,000 barrels of refined product a day, all on foreign flag ships. We are also importing some 2.5 million barrels of crude oil a day into the United States, all on foreign flag ships, and 1.8 million barrels of refined product. I would ask, in making my proposal on a compromise, that your committee see what could be done immediately to get some of this cargo, both export and import, on American flag ships. I believe the subsidy differential that is already applied to the ships that are trying to get into the domestic trade would provide employment for some of this tonnage and would give us at least some light at the end of the tunnel.

I am prepared, Mr. Chairman, to work with you and this committee. Thank you.

Mr. Biaggi. Mr. Paterson.

[Statement of Mr. Paterson follows:]

STATEMENT OF JAMES F. PATERSON, VICE PRESIDENT, NATIONAL MARITIME UNION OF AMERICA, AFL-CIO

We ask that this Committee take action to prevent the implementation of the Department of Transportation's construction-differential subsidy repayment rule.

The repayment of CDS does not put these companies that are requesting to do so on the same basis as if they had never received a subsidy. First of all, these ships would not exist except for the CDS. Second, to permit the payback, as proposed, gives these companies discounted ships.

With the prohibition against awarding CDS for domestic operation well-established, the domestic operators have made substantial financial commitments. These investments will be jeopardized if the payback is permitted.

The basic incentives of the creators of the subsidy programs in the 1936 Act were to promote the American-flag merchant marine in the foreign commerce. This is contrasted sharply with what appears to be the incentives of those who want to permit the payback of these CDS funds. It appears to us that the primary objective of those within the Administration who would change the law to permit this payback is to hasten the Government's departure from the maritime promotional programs.

We know of no companies that will go bankrupt or ships that will be laid up if this rule is not put into effect. There will, however, be a number of ships laid up and the future of some companies will be jeopardized if the rule is implemented.

It is estimated that approximately 800 seamen will lose their jobs if this rule is finalized. We know of no seamen who will lose their jobs if the rule is not put into effect.

There is concern on the part of the Navy that it will lose militarily-needed "handy-sized" tankers. This concern is dismissed in DOT's comments by repeating the old wives' tale that there are effective U.S.-controlled ships available to take the place of the U.S. tankers put out of operation.

The denial of this request to payback will not impose a hardship on the companies making the request because more than half of the ships are currently employed under either a lifetime or long-term charter. The effort to transfer these ships from this secure employment to the Alaskan trade should raise many questions.

Let's direct our concern to the companies that made the investments and built the ships for operation in the domestic trade with their own money with the knowledge of what the law permitted and did not permit. While this rule may seem equitable to those few operators who made their bad business decisions, and while the rule may seem equitable to the federal government that helped finance these bad business decisions, it is hardly equitable to those companies that ventured to build their vessels for domestic trade without any federal subsidy. To change horses now in mid-stream is grossly unfair to those who have lived by the book and who in the economic climate of the maritime industry today are having a tough enough time just surviving.

The NMU, in cooperation with the companies and in an effort to assist them through the existing shipping slump, has reduced unlicensed seamen's costs by 20 to 30 percent. This is something the union has done, not because it takes any measure of satisfaction in reducing its members' wages, but because it believes it is absolutely necessary to keep the ships operating. The effects of this rule will be to negate these efforts and make us wonder why we took this action in the first place.

Approximately 50 percent of all seagoing jobs are in the domestic trade. When these ships are laid up more hardships will be perpetrated on merchant seamen. The job situation is currently at the critical stage with many seamen unable to find enough employment to maintain the necessary sailing days required for upgrading as well as welfare benefits from their union-company pension and welfare plans.

The domestic tanker industry is currently in a slump. The thing needed most is more cargo. The thing needed least is more tonnage.

On behalf of the domestic tanker fleet and the seamen who man these tankers we ask that DOT's rule to permit the payback of CDS funds so that these tankers can engage on a permanent basis in the Jones Act trade be set aside.

STATEMENT OF JAMES F. PATERSON, VICE PRESIDENT, NATIONAL MARITIME UNION OF AMERICA

Mr. **Paterson**. Yes, thank you, Mr. Chairman.

I have a prepared statement but, in the interest of expediting the hearing, and since my glasses have taken this opportunity to self-destruct, I will quote or read from a couple of the chapters here.

The NMU asks this committee to take action to prevent the implementation of the Department of Transportation's construction-differential subsidy repayment rule. We know of no companies that will go bankrupt or ships that will be laid up if this rule is not put into effect. There will, however, be a number of ships laid up and the future of some of our contract companies jeopardized if the rule is implemented.

It is estimated that approximately 800 seamen will lose their jobs if this rule is finalized. We know of no seamen who will lose their jobs if, in fact, this rule is not put into effect.

The denial of this request to pay back will not impose a hardship on those companies making the request because more than half of the ships are currently employed either under a lifetime or a long-term charter.

The NMU is cooperating with our contract tanker companies and, in an effort to assist them through an existing shipping slump, has reduced the unlicensed seamen's cost by 20 to 30 percent. This is something that the NMU has done not because it takes any measure of pleasure and satisfaction in reducing its members' wages, but because it believes it is absolutely necessary to keep the ships operating, and that the effects of this rule will be to negate those efforts and make us wonder why we took this action in the first place.

Approximately 50 percent of all seagoing jobs are in domestic trade. When these ships are laid up, more hardships will be perpetrated on merchant seamen. The job situation is currently at a critical stage with many seamen unable to find enough employment to maintain the necessary sailing days required for upgrading as well as for pension and welfare benefits.

The domestic tanker industry is currently in a slump. The thing needed most is more cargo. The thing needed least is more tonnage.

With regard to a compromise, we have some problems, Mr. Chairman. If a man is beating me on the head, I want him to stop—not compromise and hit me with every other punch. However, apparently we are faced with a situation where something, these rules, probably will be implemented on June 6. If nothing else, NMU are realists. We would be prepared to look at a compromise that would in some way protect our members' jobs.

We work on the assumption that halitosis is better than no breath at all. [Laughter.]

Thank you, Mr. Chairman.

Mr. BIAGGI. Sometimes. [Laughter.]

But we agree. We appreciate the spirit in which you have made your statement, and really compromise was what we had been seeking for some time.

Of course, we are concerned about jobs. We are concerned about the industry. We are concerned about all the things that flow from this very precipitous action.

But when you are almost looking at the inevitable, you try to find an alternative that will be less painful. That is what we are looking at.

I appreciate the commitment on the part of Mr. Drozak and you, Mr. Paterson, to try to compromise. We will try to do that. We will try to do it.

I sincerely hope when we put something together we will have some degree of support, at least from one side if not the other. I think there is going to be a divided house; there is a divided industry. They have the administration on one side. It is not going to be an easy fight to wage, but it is one I think we must.

Ms. Mikulski.

Ms. MIKULSKI. Mr. Drozak, you talked about the lean years with our seafarers, which I would concur with. If this DOT rule goes through, what do you think it will cost, what the job impact of it would be? Do you think it would be a negative, a plus, a wash?

Mr. DROZAK. We estimate anywhere from 1,000 to 1,500 jobs in the seagoing industry.

Ms. MIKULSKI. That you would gain or lose?

Mr. DROZAK. We would lose if this rule goes through.

Ms. MIKULSKI. You would lose 1,500 more jobs?

Mr. DROZAK. 1,000 to 1,500; yes, Madam.

Ms. MIKULSKI. During the rulemaking process that did not include a public hearing, was the SIU asked for an impact statement and did you submit any testimony to DOT?

Mr. DROZAK. Yes; we did. We submitted testimony opposing the rulemaking, opposing the CDS payback, I think some about 23 pages of it, pointing out the impact that it would have on not just the seamen but the shipbuilding, the repair, the maintenance base in this country, the suppliers. A ship does a lot of things for a lot of people other than just carry crude oil or cargo. It helps survive a community.

For example, Madam Chairman, you know in Baltimore what it does. If you have ships running regularly out of Baltimore or any other place, it creates millions of dollars of revenue to the city and to the State and also to the Federal Government.

A ship is important, particularly an American flag ship, which does spend its money in the United States where a foreign ship does not.

Ms. MIKULSKI. I know what it does for a community. As you know, I live in the Fells Point area in which so many merchant seamen have come from. Not only are they great Americans and great taxpayers, but while they are paying taxes they are not home using city streets or anything else; they are out at sea earning more money to pay more taxes. [Laughter.]

So we think you're great.

Mr. DROZAK. They are good, patriotic Americans.

Ms. MIKULSKI. You are only home in time to have a few more little merchant mariners coming along. [Laughter.]

Mr. DROZAK. And they love you, Congresswoman. [Laughter.]

Ms. MIKULSKI. Given this, over the past, say, 3 years, how many jobs has SIU lost generally?

Mr. DROZAK. SIU has lost 40 percent of its jobs in the last 3 years.

Ms MIKULSKI. Forty percent.

Mr. DROZAK. When this administration came into office, we had 312 ships on American flag and all of them running. Today, I believe, the SIU has 161 ships under American flag—or only half of what we had in 1980. All of that has had an impact on our self-insured welfare and pension plans. It also, as you know, Madam Chairman, has had an impact on us because of the closing of the USPH hospital.

Ms. MIKULSKI. Yes.

Mr. DROZAK. We have had to assume all of that.

You know, during the period of time, as the NMU testified here, we have reduced the cost to the operator by some 40-odd percent.

I was interested in Congressman Lent's question this morning about what does all of this mean to the consumer. I don't see the consumer benefiting anything of the reduction of the cost of operating those ships by some 40-odd percent in the last 3 years. If anything, they have seen an increase. I make this point because what the administration people said this morning, it doesn't hold water with me. Certainly the consumer is not going to benefit by it.

Ms. MIKULSKI. Mr. Drozak, those comments are eloquent enough. I have no other questions.

I thank you for the spirit in which you came to this committee and offered a compromise. Thank you very much for your testimony.

Mr. Chairman, I have no further questions.

Mr. Biaggi. Thank you very much, gentlemen.

[Whereupon, at 3:36 p.m., the subcommittee recessed to reconvene at the call of the Chair.]

[The following was submitted for the record:]

Draft Bill A—The Biaggi Bill

That section 506 of the Merchant Marine Act, 1936 (46 App. U.S.C. 1156) is amended as follows:

(1) after "Sec. 506." insert "(a)".

(2) add the following new subsections:

"(b) The owner of a liquid bulk cargo vessel for which a construction-differential subsidy has been paid may operate that vessel in the domestic trade under the following conditions:

"(1) The owner of the vessel shall pay to the Secretary, within one year of enactment, an amount determined in accordance with paragraph (5), with interest comparable to interest on mortgages for similar ships in the coastwise trade from the earliest date of payment of the subsidy until the date of repayment.

"(2) The vessel may not be operated in the domestic trade for more than one year in a two-year period: Provided however, That two successive years of operation in the domestic trade within a four-year period shall be permitted.

"(3) Within 60 days after receipt of the payment specified in paragraph (1) of this subsection, the Secretary may, if necessary to promote competition or to avoid overcapacity, issue an order designating the years during which the vessel may operate in the domestic trade.

"(4) The vessel may not be paid an operating-differential subsidy under title VI of this Act during the period it operates in the domestic trade.

"(5) The amount of construction-differential subsidy paid on the vessel shall be apportioned over the 20-year economic life of the vessel. The amount of construction-differential subsidy paid by the owner of the vessel to the Secretary shall be one-half of the amount apportioned from the date of repayment to the end of the vessel's economic life.

"(c) Any funds repaid under subsection (a) or (b) of this section shall be used for ship construction under title V of this Act.".

Draft Bill B—The Jones Bill

AMENDMENT TO SECTION 506 OF THE MERCHANT MARINE ACT, 1936 TO PERMIT PERMANENT PAYBACK OF CDS

Section 506 of the Merchant Marine Act, 1936 (46 App. U.S.C. 1156), is amended by—

(1) after "506." insert "(a)"; and

(2) strike the 2, 3 and 4th sentences and add at the end the following new subsections.

"(b) Except as provided in subsection (a) of this section and notwithstanding section 805 of this Act, a vessel for which a construction-differential subsidy has been paid may operate in the coastwise trade for not more than 6 months in any year only if—

"(1) the Secretary decides that the operation in the coastwise trade is necessary or appropriate to carry out the purposes of this Act; and

"(2) the owner agrees to pay the Secretary—

"(A) an amount that bears the same proportion to the construction-differential subsidy paid by the Secretary as the temporary period bears to the entire economic life of the vessel; and

"(B) interest on that amount at the interest rate of loans guaranteed under title XI of this Act on the date the vessel was built.

"(c)(1) Except as provided in subsection (a) of this section and notwithstanding section 805 of this Act, after the owner of a vessel pays back a proportional amount of the vessel's construction-differential subsidy under subsection (b) of this section, the vessel may continue uninterrupted service in the coastwise trade only if the owner continues to pay back the amount required under subsection (b)(2).

"(2) Within 2 and one-half years after the date the vessel is allowed to enter the coastwise trade under paragraph (1) of this subsection, the owner of a vessel may file a notice of harm with the Secretary if that owner's vessel—

(A) was built without construction-differential subsidy;

(B) was engaged in the coastwise trade on the date of enactment of this subsection; and

(C) has not reached the end of its economic life.

"(3) A notice of harm may not be filed by a vessel owner within 6 months from the date the Secretary has made a determination under paragraph (2) of this subsection on a previous notice of harm filed by that owner.

"(4) Except as provided in this section, if the owner of a vessel proves to the satisfaction of the Secretary, in the notice of harm, that the owner's vessel cannot compete in the coastwise trade due to the continued operation of the vessel built with subsidy, the vessel built with subsidy may not be operated in the coastwise trade.

(5) After 3 years of uninterrupted service in the coastwise trade, a vessel built with subsidy may operate permanently in the coastwise trade only if the owner pays back within one year—

"(A) an amount that bears the same proportion to the construction-differential subsidy paid by the Secretary as the remaining economic life of the vessel bears to the entire economic life of the vessel; and

"(B) interest on that amount at the interest rate of loans guaranteed under title XI of this Act on the date the vessel was built.

"(d) Operating-differential subsidy may not be paid to a vessel owner for a vessel for which the construction-differential subsidy is repaid under this section for the period during which the vessel engaged is in the coastwise trade.".

99TH CONGRESS
1ST SESSION
H. R. 2485

To provide for the equitable repayment of construction-differential subsidy.

IN THE HOUSE OF REPRESENTATIVES

MAY 14, 1985

Mr. BIAGGI introduced the following bill; which was referred to the Committee on Merchant Marine and Fisheries

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A BILL

To provide for the equitable repayment of construction-differential subsidy.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 506 of the Merchant Marine Act, 1936 (46 App. U.S.C. 1156) is amended as follows:

(1) after "SEC. 506." insert "(a)".

(2) add the following new subsections:

"(b) The owner of a liquid bulk cargo vessel for which a construction-differential subsidy has been paid may operate that vessel in the domestic trade under the following conditions:

"(1) The owner of the vessel shall pay to the Secretary, within one year of enactment, an amount determined in accordance with paragraph (5), with interest comparable to interest on mortgages for similar ships in the coastwise trade from the earliest date of payment of the subsidy until the date of repayment.

"(2) The vessel may not be operated in the domestic trade for more than one year in a two-year period: *Provided however,* That two successive years of operation in the domestic trade within a four-year period shall be permitted.

"(3) Within sixty days after receipt of the payment specified in paragraph (1) of this subsection, the Secretary may, if necessary to promote competition or to avoid overcapacity, issue an order designating the years during which the vessel may operate in the domestic trade.

"(4) The vessel may not be paid an operating-differential subsidy under title VI of this Act during the period it operates in the domestic trade.

"(5) The amount of construction-differential subsidy paid on the vessel shall be apportioned over the twenty-year economic life of the vessel. The amount of construction-differential subsidy paid by the owner of the vessel to the Secretary shall be one-half of the amount apportioned from the date of repayment to the end of the vessel's economic life.

"(c) Any funds repaid under subsection (a) or (b) of this section shall be used for ship construction under title V of this Act.".

99th CONGRESS
1st Session

H. R. 2550

To amend section 506 of the Merchant Marine Act, 1936, to permit permanent payback of construction-differential subsidy.

IN THE HOUSE OF REPRESENTATIVES

May 21, 1985

Mr. Jones of North Carolina introduced the following bill; which was referred to the Committee on Merchant Marine and Fisheries

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A BILL

To amend section 506 of the Merchant Marine Act, 1936, to permit permanent payback of construction-differential subsidy.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

Section 1. Section 506 of the Merchant Marine Act, 1936 (46 U.S.C. 1156), is amended by—

(1) after "506." inserting "(a)";

(2) striking the second, third, and fourth sentences; and

(3) adding the following new subsections:

"(b) Except as provided in subsection (a) of this section and notwithstanding section 805 of this Act, a vessel for which a construction-differential subsidy has been paid may operate in the domestic trade for not more than six months in any year only if—

"(1) the vessel is not a liner vessel;

"(2) the Secretary, following hearing, decides that the operation of the vessel in the domestic trade is necessary or appropriate to carry out the purposes of this Act; and

"(3) the owner agrees to pay the Secretary—

"(A) an amount that bears the same proportion to the construction-differential subsidy paid by the Secretary as the temporary period bears to the entire economic life of the vessel; and

"(B) interest on that amount at the interest rate of loans guaranteed under title XI of this Act on the date the vessel was built.

"(c)(1) Except as provided in subsection (a) of this section and notwithstanding section 805 of this Act, after the owner of a vessel pays back a proportional amount of the vessel's construction differential subsidy under subsection (b) of this section, the vessel may continue uninterrupted service in the domestic trade only if the owner continues to pay back at the rate required under subsection (b)(3).

"(2) Within two and one-half years after the date the vessel is allowed to enter the domestic trade under paragraph

(1) of this subsection, the owner or operator of a vessel may file a notice of harm with the Secretary if that vessel—

"(A) was built without construction-differential subsidy;

"(B) was engaged in the domestic trade on the date of enactment of this subsection; and

"(C) has not reached the end of its economic life.

"(3) A notice of harm may not be filed by a vessel owner or operator within six months from the date the Secretary has made a determination on a previous notice of harm filed by that person under paragraph (2) of this subsection.

"(4) Except as provided in this section, if the owner or operator of a vessel proves to the satisfaction of the Secretary, following hearing, that the vessel cannot compete in the domestic trade due to the continued operation of the vessel built with subsidy, the vessel built with subsidy may not be operated in the domestic trade. The Secretary shall make a determination under this paragraph within ninety days after the filing of the notice of harm.

"(5) After three years of uninterrupted service in the domestic trade, a vessel built with subsidy may operate permanently in the domestic trade only if the owner pays back within one year—

"(A) an amount that bears the same proportion to the construction-differential subsidy paid by the Secretary as the remaining economic life of the vessel bears to the entire economic life of the vessel; and

"(B) interest on that amount at the interest rate of loans guaranteed under title XI of this Act on the date the vessel was built.

"(d) Operating-differential subsidy may not be paid to a vessel owner or operator for a vessel for which the construction-differential subsidy is repaid under this section for the period during which the vessel engaged is in the domestic trade.".

SEC. 2. The effective date of this Act is September 1, 1985.

Statement of Jesse M. Calhoon, National Marine Engineers' Beneficial Association

Mr. Chairman, I am pleased to provide the following statement on behalf of the National Marine Engineers' Beneficial Association, a sea-going maritime officers union representing more than ten thousand American merchant mariners.

I wish to express my strong opposition to any and all efforts, legislative and otherwise, to restrict the implementation of Secretary Dole's rule concerning CDS payback. The various proposals in this regard that I have seen would merely serve to preserve the status quo or, in at least one case, would kill CDS payback by making it totally unattractive to any operator that might wish to take advantage of the Secretary's rule.

Mr. Chairman, this CDS payback rule has been debated for more than two year. I will not repeat every argument in its favor now. I would, however, like to emphasize several points.

I support CDS payback, above all because it will help modernize our fleet by displacing aging vessels some of whom are floating coffins waiting to sink. The Marine Electric tragedy shows what can ensue when ships are kept in service far beyond their structural lives for short-term profit, with no regard for the people that man them and the families they leave behind. Government policies and programs have encouraged continued use of these older vessels, and therefore the subsidy payback rule is an about-face long overdue.

Opponents of the plan routinely distort the facts.

They claim that it violates the Jones Act—a law I strongly support. The truth is that the vessels that seek to repay their construction subsidy are fully qualified to participate in our domestic trades. They were built in U.S. shipyards, are owned by U.S. citizens, are sailed by U.S. seamen, and fly the U.S. flag. In fact, a subsidized ship must have 100 percent U.S. components, a Jones Act ship only 50 percent. Indeed, I find it curious that many who would violate the Jones Act with the CUNARD proposal suddenly "get religion" and proclaim its sanctity when the issue moves from CUNARD to CDS payback.

Opponents also seek refuge in patriotism. The truth is that some of these opponents have used the profit from their domestic shipping operations to build foreign-flag tankers in foreign shipyards operated by foreign crews that compete directly with U.S.-flag ships in the foreign trades.

Opponents argue that the plan will seriously harm the domestic fleet by lowering the rates in the Alaskan oil trade. The truth is that after subsidy repayment with interest (an integral element of the proposal), currently subsidized tankers entering the domestic trades will be saddled with capital costs greater than those borne by comparable unsubidized tankers.

Competition will be equal. Smaller over-age tankers will be forced into retirement, but this, I believe, will strengthen our merchant fleet by making it more modern and more efficient, and it will result in lowering the rates for carriage of Alaskan oil and the Federal Government (which could also reduce its subsidy liabilities by more than half a billion dollars). In addition, transportation savings over the next ten years will range from $800 million to $3.5 billion.

These lower rates will also reduce the disparity between U.S.- and foreign-flag tanker rates, a disparity that creates an unnecessary burden for our industry when we must continually justify the exclusive domestic use of Alaskan oil and the importance of the Jones Act against those who understand neither the rules by which other nations play, nor the importance of a U.S.-flag merchant fleet, nor the true meaning of national security.

Opponents cite national defense, saying that smaller, over-age tankers will be forced out of business. The truth is that many of these vessels are being forced out of business anyway. They face block retirement as well as more stringent safety laws, and they must be replaced.

The Navy has recognized the problem of aging ships in its own building program. It plans to spend billions for new tankers and fleet oilers to replace vessels that are younger than those that would be displaced by CDS subsidy payback.

If these over-age tankers are of military importance (a point which many contest), then the prudent course is not to run them to the end of their structural life (at which point they are of no use to anyone) but to purchase them now on a phased basis for our reserve fleet. CDS payback thus could help prolong their life, genuinely and significantly.

In closing, I would like to make one additional point. I wish to commend Secretary Dole for continuing to support the CDS payback plan—with persistance despite formidable opposition. I believe that the future will amply demonstrate the value of her determination. CDS payback will benefit U.S. consumers; it can be used to strengthen our defense; it will add to the Treasury; and, it will mean a more modern, more efficient, and safer U.S.-flag merchant fleet. I believe it is a sound bargain for our nation.

Thank you, Mr. Chairman.

STATEMENT OF ANDREW N. GARBIS, VICE PRESIDENT, COVE MARITIME COS., INC., NEW YORK, NY

Cove Maritime Companies, Inc. expresses deep appreciation to the Chairman and the members of this Subcommittee for giving us the opportunity to express our views on proposals relating to CDS Payback.

Cove Maritime Companies, Inc. is the parent of a group of New York based companies engaged in the ownership, operation and management of unsubsidized tankers, all qualified for and primarily engaged in U.S. domestic trades.

When we testified before your Committee on March 3, 1983 our company had 11 vessels which represented an investment by Cove of almost $100 million. Now we only have 5 vessels—the rest of our ships were scrapped.

Cove Maritime Companies, Inc. made a substantial contribution to the U.S. Merchant Marine fleet. We generated employment for as many as 1500 seamen per year and paid taxes. We now employ considerably fewer people and pay less taxes.

Cove spent domestically substantial amounts of money for repairs, stores and improvements, including upgrading of its vessels. This upgrading has extended the lives of our vessels and increased their efficiency.

We believe Cove is representative of a number of unsubsidized domestic tanker owners and operators on which the DOT CDS Payback rule will have a devasting impact. Cove, together with these unsubisidized owners and operators contribute substantially to the U.S. Merchant Marine economy and provide jobs, pay taxes and purchase U.S. goods and services, as well as generate work for our domestic shipyards. These contributions to our economy by Cove and the others will be eliminated if DOT's CDS Payback rule is finally allowed.

Cove made its investments in ships relying on the long-standing "ground rules" that CDS built vessels will continue to operate in foreign trades and the Jones Act will be preserved. Cove believes that basic fairness forbids massive intrusion by CDS built vessels which will result in serious overtonnaging and the demise of our unsubsidized fleet.

Our industry is in need of stability. Continued discussions of CDS Payback in various forms creates instability. The enactment of the rule by DOT drastically changes maritime policy in effect for nearly fifty years. We believe that the DOT rule just issued abandons legislative tradition and the goals of the 1970 amendments to the Merchant Marine Act and is contrary to the intentions of Congress when it passed these amendments.

When we testified before Chairman Biaggi in March of 1983, he requested that we affirm that a CDS Payback would devastate our industry. We and others clearly advised that such a rule would be devastating. We were therefore shocked at the cavalier attitude of DOT and their comments when they issued the final rule on CDS Payback.

In its justification of the issued rule, DOT openly admitted that 13 ships and 800 jobs will be lost. Industry officials figure the results of the rule to be equivalent to 31 vessels and more than 1600 jobs for seafarers, excluding the jobs of many shoreside support function people such as ship chandlers, repair yards, agents, shipowners and staffs and the like. The DOT rule would drive most unsubsidized independent ship owners/operators out of the trade and many companies will have to go out of business completely and DOT openly admits it.

The beneficiaries of this rule are oil companies, among them two foreign oil companies, that will unquestionably gain several hundred million dollars in windfall benefits as they cancel their foreign charters on CDS vessels. These cancellations will adversely affect our balance of payments. These companies made business judgments anticipating profitable ventures. Now, DOT gives them the opportunity to correct wrong business judgments and make substantial profits at the cost of the entire American Merchant Marine, affecting thousands of people, both socially and economically, and some to a devastating degree.

During congressional hearings, DOT openly admitted that the effect of our National Defense had not been evaluated and nothing in the current justification of the rule shows that National Defense has been taken into account.

During our last testimony, Chairman Biaggi advised us that the head of the Military Sealift Command who was supposed to testify was prohibited from testifying. The Committee apparently had his statement and sentiments. We in the industry never had a chance to know them. However, based on discussions industry representatives had with military personnel at all levels and by reading various publications issued by the military, they all clearly support that the very same tankers that CDS Payback will eliminate are the tankers the Navy would desperately need in a major emergency sealift operation. We are, of course, very disappointed that no one seems to have the courage to come out and state this clearly. For the record, the military have used our ships regularly in their movements of petroleum products.

Prior to scrapping our ships MARAD representatives inspected our vessels and recommended purchase by the Government. For budgetary reasons no purchase was made by MARAD and the vessels were scrapped in foreign lands.

Our company opposed CDS Payback because we believe it will be devastating to us and other independent tanker companies. We never expected such a rule to emanate from an agency that is responsible for the promotion of our merchant marine, nor did we expect a ruling to be as damaging to so many companies and individuals in industry and labor, and also damaging to our national security and to the U.S. Treasury at the gain of just a few special interests.

Contrary to DOT's stated purpose of removing interference by the Government, the rule that was issued by DOT will have exactly the opposite effect.

Initially, DOT argued that the payback will produce some $406.8 million ready cash for the Treasury. Justification presented by DOT now clearly states that no net cash collection will be made. In fact, taking into account that the current tax laws allow accelerated write-offs of CDS Payback, DOT provides an avenue for tax shelters of profits which would otherwise be paid to the Treasury. The result of the DOT action is substantial losses to the U.S. Treasury. I am sure other parties will address Title XI Mortgage Guarantee losses which are estimated to be in the hundred of millions of dollars.

DOT states that there will be transportation economies. Any economies that may be realized will be absorbed by charterers who are capable of using our tax laws to the maximum extent. It is clear that no benefits to the consumer will be realized.

Since the proposed ruling more than 70 tankers that were vital to the Defense Department have been scrapped (replacement value more than $5 billion). About 30 more tankers will have to be scrapped if the ruling goes into force.

Many companies and individuals invested huge amounts of money and depend on our domestic shipping industry. This rule has not studied the effect to the small business, the ship chandlers, ship repairers, spare parts suppliers, equipment manufacturers, and ship agents all over the country. Equally as important, it does not take into account the fact that the capital market of our industry will be completely destroyed.

As we stated previously we oppose DOT's CDS Payback rule. We could support legislative proposals on this subject if they were even handed, protected the interest of Cove and similarly situated operators and the public interest. The bills we understand this Subcommittee is considering need substantial revisions. For instance, the bill which we have referred to as Draft Bill A appears deficient in the following respects:

1. It does not protect the unsubsidized ships in the trade because the Secretary's designation of when CDS repaid vessels may operate in the domestic trade must be done within 60 days of the repayment for conditions years away; it provides no standards by which unsubsidized vessels are afforded protection and there is no provision for unsubsidized vessel participation in the Secretary's decision.
2. Furthermore, it does not assure capital cost parity; it does not require repayment prior to entrance in the domestic trade.
3. It lowers the cost of entering the domestic trade since it requires repayment of only one-half of the unamortized CDS and it does not require continuously compounded interest repayment.
4. Finally it does not prohibit the use of a note, ODS buy-out or Title XI financing for CDS repayment. Nor does it require cancellation of ODS; it allows those who have already been helped by the Government subsidies to move between subsidized and unsubsidized trades creating instability for the unsubsidized vessel and windfall profits for the subsidized vessel.

With respect to Draft Bill B we wish to make the following comments:

1. We are of course opposed to the DOT CDS Payback rule. We, however, recognize the efforts to find an equitable solution.

2. It is not clear to us whether all unsubsidized vessels regardless of size could participate in the Secretary's initial determination that the admission of the CDS vessel is necessary or appropriate to carry out the purpose of the Act.

3. Other difficulties we have with this bill are:

(a) a vessel laid-up at the time of enactment may not be eligible to protest because it is not at the time of enactment "engaged in the coastwise trade";

(b) it is not clear that a "suitable vessel" standard will not be used to bar protests by small vessels against large vessels;

(c) vessels beyond the end of their economic life may not protest. How rebuilt ships are to be treated is not clear. Who determines economic life?

(d) the Secretary's finding justifying the initial admission of the CDS vessel may effectively bar a later protest;

(e) linking the inability to compete to the admission of a particular CDS vessel may require a virtually impossible burden of proof, especially considering the indirect nature of the bumping process;

(f) the Secretary could delay ruling on the protest, meanwhile the CDS vessel is in the trade;

(g) the bill does not identify the period for which interest is payable nor does it provide that the interest is continuously compounded;

(h) the standard of inability to compete is vague. Literally speaking, a vessel may always be able to compete, but it may not be able to secure employment; and

(i) CDS owners may enter charters at sacrificed rates for the first three years to buy permanent coastwise rights.

In conclusion, we respectfully request that the Subcommittee take appropriate steps to have the DOT rule on CDS Payback cancelled and also we respectfully request that you take all necessary actions to secure stability for the unsubsidized tanker owners and the U.S. Merchant Marine by precluding any form of CDS Payback.

STATEMENT OF CROWLEY MARITIME CORP.

Crowley Maritime Corporation is a U.S.-flag, U.S.-citizen-owned company engaged in the transportation of cargo of all types between points in the United States and would like to take this opportunity to present its views on H.R. 2550 introduced by Congressman Jones on May 21, 1985, and H.R. 2485 introduced by Congressman Biaggi on May 14, 1985, both of which would amend Section 506 of the Merchant Marine Act, 1936, in certain respects. Crowley is particularly concerned about the types of vessels covered by the bills and provisions waiving the applicability of Section 805 of that Act. Crowley opposes any extension of the right to pay back CDS beyond tankers and any exemption from the requirements of Section 805.

Secretary Dole recently promulgated a rule under which a tanker built with CDS may pay back all CDS, with interest, and thereupon enter the coastwise trade without restriction as to whether there is competitive harm to existing carriers or as to the period or area of operation. However, all types of vessels except tankers are excluded from the scope of the rule. Further, the rule does not eliminate the requirements of Section 805(a), requiring operators receiving operating-differential subsidy to apply to the Secretary of Transportation for approval for any coastwise operations.

Congressman Biaggi's bill is limited to "liquid bulk cargo vessels" and Congressman Jones' bill requires that "the vessel is not a liner vessel". Crowley strongly opposes any amendment to either of these bills which would permit CDS payback on vessels other than tankers. Although CDS payback for tankers has been the subject of a lengthy debate here in Congress and at the administrative level, there has never been any showing that a CDS payback program for liners has merit or will produce any benefits similar to those claimed for payback of CDS on tankers. Indeed, Crowley operates in Alaska and Puerto Rico trades and could be severely damaged if CDS-built liners were permitted to repay their subsidy and enter that trade. It would be paradoxical for Congress to enact legislation whose primary purpose was to restrict the access granted by Secretary Dole's rule to CDS-built tankers, and at the same time provide for CDS payback for liner vessels not even included in that rule.

Congressman Jones' bill would limit access to the coastwise trade for any CDS built vessel to an initial three years and thereafter restrict access if a vessel built without CDS shows an inability to compete due to the presence of the CDS-built vessel. It further provides specifically that during the three year period before a vessel becomes eligible for the total pay back of CDS its terms apply "notwithstanding Section 805 of this Act". Thus, it appears that a CDS-built vessel the owner of which was affiliated with an owner or operator of vessels receiving ODS would be permitted to enter the coastwise trade immediately.

Crowley opposes any bill abrogating Section 805(a). That section has accomplished its purpose since it was enacted. It is not an absolute prohibition. It bars companies receiving ODS from also competing in the coastwise trade only if their competition is unfair or if some other policy of the Act is violated. Operators in the Hawaii, Alaska and Puerto Rico trades have made huge investments in their fleets. Recently, as a result of deregulation, rates have fallen in these trades.

In sum, Crowley urges this Committee to limit all legislative initiatives to the payback of CDS on tankers, the issue decided by Secretary Dole.

STATEMENT OF JOHN J. ERVIN, EXECUTIVE VICE PRESIDENT, TRINIDAD CORP.

This statement is being submitted in lieu of testimony to be considered as part of the official record on the hearings of the Subcommittee for the payback of Construction Differential Subsidies (CDS) by tank vessels.

Trinidad Corporation, a subsidiary of Apex Holding Company owns a majority interest in Glacier Bay Transportation Corporation, the bareboat charterers of the SS *Glacier Bay*, 80968 Deadweight.

This vessel was constructed in 1970 specifically for the Alaskan trades, and was extensively modified in 1981 to conform to the requirements of the Port and Tanker Safety Act of 1978. It has operated exclusively in these trades from the startup of operations of the Trans Alaskan Pipeline until December 1984 when it was released from charter. This release from charter coincided with the entry into the Alaskan trades two (2) subsidized tankers for six (6) month service under Section 506 waivers. Upon release from charter, the vessel has been unemployed except for a single voyage Public Law 480 grain cargo to Pakistan. The vessel has no charter commitments after the current grain charter in spite of our continued efforts to seek employment.

The difficulties that we are presently experiencing on the *Glacier Bay* in our efforts to seek employment because of the unwarranted Section 506 waivers in November/December 1984, will only be aggravated and be made permanent by the adoption of any rule or enactment of any law to permit the payback either totally or partially of Construction Differential Subsidies (CDS).

These hearing are being held to review various alternative proposals to permit owners of CDS vessels to enter the Jones Act trades at a time when substantial numbers of unsubsidized vessels are idle for lack of any employment opportunities, and several other modern unsubsidized vessels such as our *Glacier Bay* can only obtain marginal employment at far less than compensatory rates.

Since the enactment of the 1970 amendments to the Merchant Marine Act of 1936, Owners have had the right to freely choose to construct U.S. Flag bulk carriers for service in either the Jones Act (unsubsidized) or on U.S. foreign (subsidized) trades. Each of these prospective Owners, including ourselves, made our decisions based on individual evaluations of market prospects for the projected period of financial risk on the vessel(s). In each such decision, the risk of error and financial consequences must be considered.

The impact of any change to permit the payback of CDS will obviously shift the financial burden of the present Owners of CDS vessels to the Owners of unsubsidized vessels as a result of excess capacity and the inevitable increase in layup of these vessels for the foreseeable future.

To the extent that your Committee finds it necessary to adopt legislative changes to the existing laws, it should do so only with the utmost care to assure that such changes do not extend a windfall and/or a free license to the Owners of subsidized vessels to enter the Jones Act trades. It is also important that the financial burden of their investment decisions are not shifted to the unsubsidized Owners.

Any rule or legislative changes that would permit the payback of CDS should include the following conditions:

(1) require full repayment of the unamortized balance of the CDS plus fully compounded interest at the time of granting permission to enter into the Jones Act trades;

(2) prohibit the use of Title XI for the financing of any such paybacks;

(3) prohibit the cancellation of any existing charter or such vessel(s) that were executed at the time of granting of subsidies on these vessel(s);

(4) establish a definite period for such paybacks to avoid the establishment of a free continuous license for possible entry into the Jones Act trades.

The affect of any change with respect to the payback of CDS and termination of Operating Differential Subsidies extends a "second chance" for the owners of such vessels to reassess these individual investment opportunities and change them as they consider it desirable. If your committee finds it necessary to take such action, it should also extend a similar "second chance" to the present owners of unsubsidized vessels. This can be accomplished by providing for a one time choice on the part of owners of unsubsidized vessels to have the Maritime Administration pay off all outstanding indebtedness on such vessel(s) in exchange for the transfer of title of these vessels to that agency. This would give the unsubsidized Owners an opportunity to relieve themselves of a financial burden placed upon them as the result of the adoption of CDS payback value.

Lastly, the Committee must also consider the effect of the adoption of any CDS payback policy on the further decline of our Merchant Marine and its projected role in any national emergency.

Tanker Management Inc.,
New Orleans, LA, May 15, 1985.

Hon. Mario Biaggi,
Chairman, U.S. House Subcommittee on Merchant Marine, Washington, DC.

Dear Congressman Biaggi: Tanker Management Inc. (TMI) is the Demise Charter Owner of four U.S. flag tank vessels and the operator of two of them. We are concerned for our corporate future because of the recent actions by the Secretary of Transportation to permit the payback of construction differential subsidies (CDS) by tank vessels. There have been several studies made by different industry groups estimating the number of ships that might elect to repay their subsidy and join the Jones Act fleet. These various studies have differed on the impact these vessels would have on the current Jones Act fleet, however, it is clear that it will be adverse; only the severity of the impact varies among the studies.

It is our belief that sanitized former CDS vessels will not cause a measurable difference in current tanker market rates, but will drastically alter the present constituency of the tanker companies from those of us currently participating in the Jones Act trade, to those who originally chose to ply the foreign trade. Tanker market rates will drop slightly lower than their current depressed rates. There exists a considerable surplus of tonnage which forces tanker rates to barely cover operating costs. Additional new tonnage will reduce that rate to something above vessel layup costs, but below minimal operating costs.

It is our belief that some current Jones Act operators will be unable to continue operations after CDS vessels are allowed into Jones Act trade. Admittedly, some CDS operators may find that they cannot get charters and may also face economic hardship. I question the wisdom in destroying us all.

Tanker Management Inc. urges you and the Subcommittee on Merchant Marine to work to counter the Secretary's actions permitting CDS repayment of tankers.

Very truly yours,

Robert W. Carson,
President.

U.S. House of Representatives,
Committee on Merchant Marine and Fisheries,
Washington, DC, May 21, 1985.

To: Members, Subcommittee on Merchant Marine.
From: Majority and Minority Staff.
Subject: May 23, 1985 hearing on legislation dealing with the payback of construction-differential subsidy (CDS) to permit admission of CDS-built vessels to the domestic-coastwise trade.

ISSUE

Title V of the 1936 Merchant Marine Act established the Construction-Differential Subsidy (CDS) program, which pays the cost difference of constructing a vessel in a domestic shipyard. Vessels built with CDS are prohibited from participating in the coastwise (Jones Act) trade. An exception to this prohibition is contained in section 506 of the Merchant Marine Act, 1936, (as amended). The exception provides that vessels built with CDS may enter the coastwise trade for six months in any year if the Secretary of the Department of Transportation (DOT) approves, and the operator repays a pro rata portion of the CDS for the period of operation in the coastwise trade. Under the regulations, interest on repaid CDS is not required and has not been imposed.

On May 7, 1985, DOT issued a final rule. The rule would allow an operator of any liquid bulk cargo vessel built with CDS, to permanently enter the vessel in the Jones Act trade upon repayment of the unamortized portion of the CDS paid, plus compounded interest. This authority is effective for one year beginning June 6, 1985. The money due would have to be repaid within this year. The requirement for payment of compounded interest is an attempt by DOT to mitigate harm to and objections by the domestic operators. They say that repayment of only the unamortized portion of CDS paid will leave the operators of CDS-built vessels with a competitive advantage. DOT views the final rule as a fair compromise. However, domestic operators still object, alleging that the rule will result in substantial overcapacity that will ultimately drive them out of business.

LEGISLATIVE PROPOSALS

H.R. 2485

Two legislative approaches to CDS repayment have been suggested. They are H.R. 2485, introduced by Chairman Biaggi and H.R. 2550, introduced by Chairman Jones.

The intent of H.R. 2485 is to reduce by half the amount of CDS-built tonnage that would enter the domestic trade under the proposed rule, by generally limiting the time each vessel can participate in the trade to one year out of two.

H.R. 2485 provides that CDS-built vessels may enter the Jones Act trade on the following conditions:

Repayment of one-half of the unamortized CDS paid for the vessel.

Payment of interest at a rate comparable to rates on mortgages on similar ships in the domestic trade.

Operation in the domestic trade for not more than one year in a two-year period; two successive years of operation in a four-year period is permitted.

The Secretary may issue an order designating the periods of operation.

No operating-differential subsidy (ODS) shall be paid for such periods of operation.

H.R. 2550

H.R. 2550 continues the present six month waiver provision, with the imposition of interest. In addition, an operator of a CDS-built vessel would be permitted to obtain consecutive six month waivers.

Specifically, H.R. 2550 provides for CDS repayment as follows:

Owner can operate in domestic trade for three years with pro rata payback of CDS in six month increments, with interest at rate of title XI loans at time vessel was built.

During the two and a half years after CDS vessel is allowed in trade it may be required to justify the continued permission every six months, if a non-CDS vessel files notice of harm.

The vessel filing the notice of harm must be engaged in domestic trade on date of enactment, and be less than 20 years of age.

After Secretary has ruled, another notice of harm may not be filed for six months.

If Secretary rules for the non-CDS vessel, the CDS vessel may not operate in domestic trade.

After three years of uninterrupted service in domestic trade, CDS vessel may operate permanently in trade if: CDS is repaid in an amount that bears same proportion to CDS paid for the vessel as remaining economic life bears to entire economic life, and interest is paid at rate of title XI loans at time vessel was built.

No ODS.

BACKGROUND

Merchant Marine Act of 1936.—Section 506 of the Merchant Marine Act of 1936 (Appendix 1) provides that every U.S.-flag vessel operator receiving CDS must agree that the vessel will be used exclusively in the foreign commerce.

However, the Maritime Administration may permit a subsidized operator to enter the Jones Act trade for a period not to exceed six months in any one year if the Secretary determines "that such transfer is necessary or appropriate to carry out the purposes of this Act." This waiver of the section 506 prohibition is conditioned on the operator repaying the construction subsidy on a pro rata basis and giving up ODS for that period.

Statutory law does not specifically address whether a vessel built with CDS may be permanently admitted to the Jones Act trade.

Seatrain Shipbuilding Corp. v. *Shell Oil Co.*, 444 U.S. 573 (1980)

In 1969, Seatrain contracted to build a 225,000 d.w.t. supertanker with CDS and title XI financing. When this tanker, the *Stuyvesant*, was completed in 1977 there was significant overtonnaging in the world tanker market and it was clear that the *Stuyvesant* could not economically compete on the world market. However, by 1977 there was a significant increase in the demand for tankers to transport Alaskan oil to the lower 48 States. This trade was not affected by the world overtonnaging since foreign tankers are excluded by the Jones Act.

In light of these economic realities, the owners of the *Stuyvesant* offered to repay their subsidy in full in exchange for permission to permanently enter the Jones Act trade. This offer was accepted by the Secretary of Commerce (then the Cabinet officer involved). Subsequently, competitors of the *Stuyvesant* brought a lawsuit alleging that the Secretary had acted improperly and beyond the scope of the section 506 exemptions. The case eventually reached the Supreme Court, which found that Congress had not specifically prohibited the permanent transfer of CDS vessels into the domestic trade and the Secretary could grant such a transfer under his broad authority to promote the U.S. merchant marine.

MARAD REGULATIONS

The District Court decision, *Alaska* v. *Kreps*, 595 F.2d 1814 (D.C. Cir. 1979), which preceded *Seatrain* v. *Shell* held that MARAD's action, admitting the STUYVESANT without an accompanying economic analysis, was an abuse of discretion. The court also urged MARAD to establish guidelines and procedures applicable to the permanent waiver of domestic trading restrictions so as to ensure a fair opportunity for public and industry comment and equal treatment for all applicants.

Since 1978, MARAD has issued four different sets of proposed and interim rules dealing with procedures governing CDS paybacks. The final rule, issued on May 7, 1985, considered comments on a proposed rule published for comment by DOT on January 31, 1983. This proposed rule was the subject of Subcommittee hearings on March 3, 1983 and May 23, 1984. In addition, the Department of Transportation was placed under certain legislative prohibitions relating to the proposed rules. These are found in P.L. 98-78 (DOT FY 84 appropriation), P.L. 98-166 (MARAD FY 84 appropriation), and P.L. 98-411 (MARAD FY 85 appropriation). The prohibitions are no longer operative. The relevant provisions are attached as Appendix 2.

ECONOMIC IMPACT OF CDS REPAYMENT

Under the final rule, a maximum of 28 CDS tankers would be eligible to repay their CDS and enter the Alaskan trade full time. DOT has predicted seven VLCC's are likely to repay. They also speculate that six Panamax tankers might repay but think it not likely due to economic conditions. If allowed into the trade full time, the 13 vessels would add 2.3 million d.w.t. capacity.

The unsubsidized U.S.-tanker fleet consists of 210 tankers of 10.4 million d.w.t. About 5.8 million d.w.t. were used in Alaska during 1984.

Jones Act operators continue to believe that the admission of the CDS-built vessels to the domestic trade could lead to severe overtonnaging and result in non-compensatory rates. Subsidized operators argue that there is a need for additional tonnage in the trade and that the admission of subsidized vessels would merely "bump" less efficient operators out of the trade.

DOT estimates that the Treasury would realize up to $277 million if the seven VLCC's were to repay CDS. Under the Biaggi bill, CDS repayment for the seven VLCC's could still generate revenues of approximately $139 million including interest for ship construction projects. No estimates of CDS repayment are available with respect to Mr. Jones' bill.

In addition, the CDS-built tankers now receiving ODS would no longer be eligible for ODS.

TITLE XI

The title XI loan guarantee program has insured obligations in excess of $200 million on the 13 vessels that may enter the domestic trades.

However, the title XI exposure would rise if MARAD were to extend loan guarantees to cover repayment of CDS. (The proposed regulations imply that title XI would be available to help finance repayment.) With the entry of CDS-built vessels, there is the possibility that domestic tankers with title XI obligations would also be unable to find work and the guarantees could be called in by the loan holders.

CONCLUSION

The primary issue before the Subcommittee is whether, and under what circumstances, permanent repayment should be permitted. The DOT rulemaking is already the subject of a court challenge by opponents of repayment. Language prohibiting enforcement of a final rule was approved on May 21, 1985 at the markup of the Fiscal Year 1985 supplemental appropriations measure considered by the Appropriations Committee. The two bills under consideration represent alternative approaches to changing statutory law, to finally resolve the issue.

Members, Committee on Merchant Marine and Fisheries.

Appendix 1

MERCHANT MARINE ACT, 1936

Section 506. Every owner of a vessel for which a construction-differential subsidy has been paid shall agree that the vessel shall be operated exclusively in foreign trade, or on a round-the-world voyage, or on a round voyage from the west coast of the United States to a European port or ports which includes intercoastal ports of the United States, or a round voyage from the Atlantic coast of the United States to the Orient which includes intercoastal ports of the United States, or on a voyage in foreign trade on which the vessel may stop at the State of Hawaii, or an island possession or island territory of the United States, and that if the vessel is operated in the domestic trade on any of the above-enumerated services, he will pay annually to the Commission that proportion of one twenty-fifth of the construction-differential subsidy paid for such vessel as the gross revenue derived from the domestic trade bears to the gross revenue derived from the entire voyages completed during the preceding year. The Commission may consent in writing to the temporary transfer of such vessel to service other than the service covered by such agreement for periods not exceeding six months in any year, whenever the Commission may determine that such transfer is necessary or appropriate to carry out the purposes of this Act. Such consent shall be conditioned upon the agreement by the owner to pay to the Commission, upon such terms and conditions as it may prescribe, an amount which bears the same proportion to the construction-differential subsidy paid by the Commission as such temporary period bears to the entire economic life of the vessel. No operating-differential subsidy shall be paid for the operation of such vessel for such temporary period.

Appendix 2

P.L. 98-78 section 315 provides:

None of the funds provided in this Act for the Department of Transportation shall be used for the enforcement of any rule with respect to the repayment of construction-differential subsidy for the permanent release of vessels from the restrictions in section 506 of the Merchant Marine Act, 1936, until 60 days following the promulgation of any such rule.

Notwithstanding any other provision of law, the enforcement of any rule regarding the repayment of construction-differential subsidy for the permanent release of vessels from the restrictions in section 506 of the Merchant Marine Act, 1936, shall be held in abeyance for at least 60 days from the date of enactment of this Act.

P.L. 98-166 provides:

None of the funds provided in this Act for the Maritime Administration shall be used for enforcement of any rule with respect to the repayment of construction-differential subsidy for permanent release of vessels from the restrictions in section 506 of the Merchant Marine Act, 1936, as amended, until June 15, 1984.

P.L. 98-411 provides:

None of the funds provided in this Act for the Maritime Administration shall be used for enforcement of any rule with respect to the repayment of construction-differential subsidy for permanent release of vessels from the restrictions in section 506 of the Merchant Marine Act, 1936, as amended, until May 15, 1985.

APPENDIX 3

REGULATIONS GOVERNING CDS PAYBACKS

The District Court decision, *Alaska* v. *Kreps,* 595 F.2d 1814 (D.C. Cir. 1979), which preceded *Seatrain* v. *Shell* held that *Marad's* action, admitting the *Stuyvesant* without an accompanying economic analysis, was an abuse of discretion. The Court also urged *Marad* to establish guidelines and procedures that would be applicable to CDS repayment and permanent waiver of domestic trading restrictions so as to ensure a fair opportunity for public and industry comments to be heard and to ensure equal treatment for applicants.

In 1978, *Marad* issued a notice of proposed rulemaking (43 FR 51045; November 2, 1978) that would have added a new provision to its regulations (46 CFR 276.3) describing its policy for considering all applications for the total repayment of CDS. At the time the proposal was published, the *Stuyvesant* litigation still had not been resolved. However, once the Secretary's discretion to allow permanent release was affirmed by the Supreme Court, the proposal was republished for comment in May 1980 (45 FR 29610; May 5, 1980). The only provision new to the republished version was that total CDS repayment would be "plus interest."

At the time of the republication of the proposed rule, charterers and owners of six ships built with construction susidies made application for CDS repayment. One of those was for the *Bay Ridge,* another Seatrain vessel. On October 15, 1980, *Marad* adopted and made immediately effective an interim rule to govern applications for CDS repayment (45 FR 68393). The interim rule differed from the proposed rule in that it was narrower in scope, but it retained greater discretion on the part of Marad to determine whether to grant or deny applications for CDS repayment. Approvals would be granted only for vessels of at least 100,000 d.w.t.

On November 13, 1980, *Marad* approved the *Bay Ridge* application and deferred other applications.

On November 15, 1980, the Independent U.S. Tanker Owners Committee (ITOC) filed a complaint alleging substantive and procedural defects. The District Court granted summary judgment for defendants on all counts from which an appeal was taken.

In *Independent U.S. Tankers Owners Committee* v. *Drew Lewis,* No. 81-2121 (D.C. Cir., September 7, 1982), the Court vacated the interim rule on procedural grounds. It concluded that the rule lacked a general statement of basis and purpose. Moreover, the Court criticized *Marad* for not discussing or responding to filed comments and for not explaining why it retained so much discretion in deciding on applications as opposed to promulgating more outcome-oriented and specific rules.

On January 31, 1983, DOT issued a Notice of Proposed Rulemaking that would have applied to all tanker vessels, but also invited comment on limiting the rule to tankers of at least 100,000 d.w.t. or some lower weight.

On February 2, 1983, ITOC sued the Secretary of Transportation in U.S. District Court for the District of Columbia to enjoin further proceedings under the proposed rulemaking. ITOC contended that the Secretary of Transportation had entirely bypassed *Marad* by commencing his own rulemaking proceeding, after having delegated authority to *Marad.* The District Court upheld the Secretary's power to promulgate rules. This opinion was appealed to the U.S. Court of Appeals, D.C. Circuit. The Court of Appeals denied the petition on May 2, 1983.

[From the Congressional Record, May 14, 1985]

INTRODUCTORY STATEMENT TO H.R. 2485

REPAYMENT OF CONSTRUCTION-DIFFERENTIAL SUBSIDY

HON. MARIO BIAGGI

OF NEW YORK

IN THE HOUSE OF REPRESENTATIVES

Tuesday, May 14, 1985

Mr. BIAGGI. Mr. Speaker, I rise to introduce legislation dealing with the repayment of construction-differential subsidy.

From 1936 to 1981, this program subsidized the cost of constructing vessels for the foreign trade so that U.S. operators could obtain their vessels at approximately the same cost as their foreign competitors. Since there is no foreign competition for the carriage of goods between U.S. ports, these subsidized vessels were excluded from the domestic trade, except in very narrow circumstances for short periods of time.

In the 1970's, the Maritime Administration approved a proposal by a subsidized company that permitted the company to repay its construction-differential subsidy and permanently operate in the domestic trade. That decision gave rise to numerous lawsuits, including a trip to the U.S. Supreme Court. However, the authority of the Government to accept repayment and permit an operator to permanently enter the trade was eventually upheld.

Last week, the Department of Transportation issued regulations that will permit all subsidized tankers to repay their construction-differential subsidy and permanently enter the coastwise trade. These subsidized tankers are suffering because of the worldwide oversupply of oil tankers. They need additional income from the domestic trade if they are to survive, however, if these vessels are permitted to enter the trade en masse the domestic operators presently in the trade allege there will be substantial overcapacity, which will drive them out of business.

In light of these very serious claims, I have scheduled a hearing of the Merchant Marine Subcommittee on May 23 to examine this matter. As a possible compromise, I am today introducing legislation that would grant the subsidized operators authority to engage in the trade for 1 year out of every 2. My hope is that by admitting the ships for limited periods of time we will minimize the damage to the domestic operators. This legislation will also benefit subsidized operators by reducing the amount they must pay by one-half and by eliminating the costly and complex ad hoc adjudicatory hearings that precede a temporary entry into the trade.

There are numerous benefits to the Federal Government and general public. The primary benefit is the payment of $200 million, which will reduce the need for additional appropriations for maritime programs. Additionally, this will reduce the Government's regulatory responsibility and ODS [operating differential subsidy] payments. Hopefully, it will result in lower transportation cost of Alaskan oil.

The Department of Transportation has expended a great deal of time and funds to develop this rule. They view it as a reasonable compromise, which takes into account the needs of both the subsidized and domestic operators. Despite their efforts to balance the competing interests, domestic operators are still objecting to the regulation. The scheduled hearing will offer an opportunity to develop an approach acceptable to all affected parties. The time to act is limited since the rulemaking will take effect in early June. As the committee deals with construction-differential subsidy repayment our goal is to develop a fair system meeting the needs of CDS and domestic operators.

[From the Congressional Record May 22, 1985]

INTRODUCTORY STATEMENT TO H.R. 2550

ORDERLY PAYBACK OF MERCHANT VESSEL CONSTRUCTION SUBSIDY

HON. WALTER B. JONES

OF NORTH CAROLINA

IN THE HOUSE OF REPRESENTATIVES

Tuesday, May 21, 1985

Mr. JONES of North Carolina. Mr. Speaker, I have today introduced H.R. 2550, a bill to provide for the payback of construction subsidy by owners of dry bulk vessels and tankers. The bill is directed toward resolving the longstanding dispute between those who built U.S.-flag ships without subsidy for service dedicated to the U.S. domestic trade and those who, with the aid of construction subsidy, built ships destined to compete with lower cost foreign-built ships in the foreign commerce of the United States.

As foreign trade for U.S. tankers and bulkers fell off in recent years, a concerted effort was made to find employment for these vessels in the booming Alaska oil trade. The device employed or proposed was the repayment of subsidy, in a lump sum, and the immediate entry of previously restricted vessels into the domestic commerce. The most recent action by the Department of Transportation was the promulgation of a rule permitting allcomers to payback and enter the domestic trade on the condition that the subsidy payback be completed within 1 year after the rule takes effect. It is assumed that the rule becomes effective on or about June 6, 1985.

The concern of many, inside and outside the Congress, has been that the unrestricted entry of large numbers of vessels, each having great capacity, would drive present operators out of the trade. Worse, these present operators would have no other employment and their disappearance would be detrimental to our sealift capacity, since many of these vessels are the very type most useful to the Navy in time of national emergency. On the other hand, the inability to find employment for the vessels wishing to repay subsidy might result in massive defaults on the debt service on these vessels, further exacerbating a very serious problem that has developed in the Nation's maritime loan guarantee program, title XI.

The bill introduced today employs a waiver device that has been in place for some time that allows the Secretary of Transportation to allow a subsidy-built vessel to repay a proportionate amount of the subsidy and enter the domestic trade for a period not greater than 6 months out of every 12. This bill merely allows extension of the 6-month period if the Secretary finds that the continued operation of that vessel would not constitute unfair competition for the nonsubsidized vessel(s) in trade, and if the vessel continues to repay proportionately its construction subsidy. Protests may be lodged by "Jones Act" operators, but not more frequently than every 6 months. At the end of 3 years of continuous operation in the domestic commerce by a subsidy-built vessel, the balance of the subsidy may be repaid, and the vessel is at that point a permanent Jones Act vessel.

I believe this bill constitutes a workable and orderly method for providing for the repayment of construction subsidy, while maintaining the integrity of the traditional "Jones Act" fleet.

STATEMENT OF JOHN C. COUCH, PRESIDENT AND CHIEF OPERATING OFFICER, MATSON NAVIGATION CO., INC.

Mr. Chairman, I appreciate the opportunity to submit the views of Matson Navigation Company, Inc. for the Merchant Marine Subcommittee's hearing record on H.R. 2485 and H.R. 2550 concerning the repayment of construction-differential subsidy.

Matson is an unsubsidized U.S.-flag, ocean common carrier primarily engaged in the transportation of containerized and containerizable cargo moving between the United States Pacific Coast and ports in the State of Hawaii. Matson provides regularly scheduled service between Seattle, Portland, Oakland and Los Angeles on the Pacific Coast and Honolulu, Kahului, Hilo and Nawiliwili in Hawaii.

For many years prior to 1980, Matson owned and operated three combination container-drybulk vessels which carried bulk raw sugar from Hawaii to a refinery in Crockett, California. Since 1980, sugar has been carried from Hawaii to Crockett by a transportation cooperative affiliated with and serving California and Hawaiian Sugar Company (C&H) in drybulk vessels which it operates or charters. Although Matson sold one of the three vessels to C&H, we occasionally carry some sugar in bulk and have an interest in increasing our bulk carriage.

My comments are limited to two aspects of H.R. 2550 which are of particular interest to Matson. First, Matson strongly supports the provisions of H.R. 2550 that would repeal the authority of the Secretary of Transportation to accept repayment of construction-differential subsidy (CDS) on dry cargo liner vessels so that these CDS liners could operate permanently in the domestic trades or could operate exclusively in a domestic trade for six-month periods. The rationale for the Secretary of Transportation promulgating the Department's recent CDS payback regulations on tankers does not apply to the liner trades. The Secretary specifically found that there is no need for a CDS payback program for liner vessels. Matson wholeheartedly supports the prohibition on CDS payback for liners resulting from the provision in H.R. 2550 striking the 2d, 3d and 4th sentences of Section 506 of the Merchant Marine Act, 1936, but we suggest that H.R. 2550 be amended to include specific language which would clarify the legislative intent on this point.

Second, Matson is opposed to the provisions of H.R. 2550 that would repeal Section 805(a) of the Merchant Marine Act, 1936, in the case of CDS payback for nonliner vessels. Section 805(a) currently makes it unlawful to pay operating-differential subsidy (ODS) if an ODS contractor or its affiliates or certain others operate any vessel in domestic intercoastal or coastwise service without written permission of the Secretary of Transportation. Specifically, the Secretary may not permit direct or indirect recipients of ODS to operate either liner or non-liner vessels in those domestic services if the Secretary finds that this operation would result in unfair competition to exclusively domestic operators or would be prejudicial to the objects and policy of the Merchant Marine Act, 1936.

Matson feels strongly that Section 805(a) should not be abrogated in any respect. Section 805(a) is not a prohibition on domestic operations by ODS recipients. Rather, it is a mechanism by which exclusively domestic unsubsidized operators can protect themselves against the possibility of ODS being used unfairly to support the operation of a competing vessel in such domestic services. Only companies that continue to receive ODS or are affiliated with a receipient of ODS will require the Secretary's approval under Section 805(a) if they wish to payback CDS on vessels which they desire to employ in such domestic service. Companies which do not receive ODS or have no ODS affiliation are not subject to 805(a) approval requirements.

Although H.R. 2550 establishes new standards which must be met before CDS may be repaid on non-liner vessels that would be employed in the domestic trades, these standards are no substitute for Section 805(a) safeguards. First, unlike the "notice of harm" provisions of H.R. 2550 which come into play after a non-liner vessel engages in domestic operations, (but only with respect to a vessel engaged in domestic trade on the date of enactment of H.R. 2550) Section 805(a) approval is required before the ODS recipient or its affiliate may commence domestic operations so that the possibility of unfair competition or a detrimental impact on existing protected services may be examined before the damage has had a chance to occur. Moreover, without Section 805(a), there is no specific statutory authority which would give unsubsidized domestic operators a forum to challenge whether ODS would unfairly spill over into the proposed domestic operation. Further, notwithstanding all of the extensive comments that were submitted to the Department of Transportation in connection with CDS payback rulemaking, we are unaware of anything in the rule or the comments that suggests the need for elimination of the requirements of Section 805(a). There is no need to tamper with this important operating-differential subsidy safeguard in connection with this legislation which is otherwise confined to construction-differential subsidy and Section 506 of the Merchant Marine Act, 1936. Bulk carriers have been subject to Section 805(a) ever since they first became eligible for operating subsidies in 1970 and have accommodated themselves to its requirements, as have the liner companies since 1936.

The importance of Section 805(a) to domestic operators has been clearly demonstrated in Maritime Administration Docket No. S-724 where several unsubsidized operators objected, under Section 805(a), to the domestic operation of a Ro/Ro vessel by an affiliate of an ODS recipient. In December 1983 the Maritime Administrator found that operation of this Ro/Ro vessel in the Puerto Rico, Alaska and Hawaii trades would have an adverse effect on existing operators and was, therefore, prejudicial to the objects and policy of the Merchant Marine Act, 1936. Permission for the domestic operation was, accordingly, denied under Section 805(a). The Administrator's decision was reversed by Secretary of Transportation Dole since the Secretary interpreted the "objects and policy" clause of Section 805(a) differently than the Administrator. The unsubsidized operators who where adversely impacted, including Matson, have filed suits in the U.S. District Court for the District of Columbia, seeking to overturn the Transportation Secretary's decision. Clearly, Section 805(a) is an extremely important safeguard for the unsubsidized domestic offshore operators. No need for its repeal has been demonstrated. Matson strongly urges that there be stricken from the bill the language in subsections (b) and (c) of H.R. 2550, which repeals Section 805(a) insofar as it applies to non-liner vessels built with CDS.

Thank you for your consideration of the views of Matson Navigation Company, Inc.

SEA-LAND CORP.,
Edison, NJ, June 13, 1985.

Hon. MARIO BIAGGI,
Chairman, Subcommittee on Merchant Marine, Committee on Merchant Marine and Fisheries, Washington, DC.

DEAR MR. CHAIRMAN: Please include these comments in the hearing record of H.R. 2485 and H.R. 2550 on the subject of repayment of construction differential subsidy. Both bills would amend Section 506 of the Merchant Marine Act of 1936 and I understand that a markup is scheduled for June 18, 1985.

As you are aware, Sea-Land Corporation is an international containerized freight transportation and trade services company. Our principal subsidiary, Sea-Land Service, Inc., is a U.S.-flag ocean common carrier in the domestic and foreign trades. Sea-Land Service operates a fleet of 59 vessels serving 106 ports in 75 countries and territories, including regular service to and from Puerto Rico and Alaska. Sea-Land Service, Inc. does not participate in the federal government's operating differential subsidy program.

We recently entered into a contract for the construction of three modern containerships to be operated in the noncontiguous domestic trades. This contract represents the only commercial construction of major liner vessels currently underway in United States shipyards. It involves an investment in excess of $180 million—or about 20 percent of our equity capital.

Sea-Land's concerns with respect to the two bills relate solely to liner services. Sea-Land strongly supports the intent of these bills to limit repayment of construction differential subsidy (CDS) to tanker and bulk vessels. Whatever the merit of CDS repayment with respect to tankers and bulk vessels, there has been no proposal or justification advanced for permitting CDS repayment on liner vessels. In fact, even the possibility of extension of CDS repayment to liner vessels deters potential investment in new U.S.-built liner vessels for the domestic trades.

Provisions of H.R. 2485 and H.R. 2550 as introduced, do not extend far enough to address adequately the intended objective of barring CDS repayment on liner vessels. This is so because the Supreme Court's decision in the *Stuyvesant* case (*Seatrain Shipbuilding Corporation, et al.* v. *Shell Oil Company, et al,* 444 U.S. 572 (1980)) held that the Secretary's broad contracting powers and discretion to administer the 1936 Act comprehended the authority to grant permanent releases from the requirement of Section 506 that subsidized vessels operate only in the foreign trades. We respectfully suggest that H.R. 2485 and H.R. 2550 be amended to specifically prohibit CDS repayment for liner vessels and specifically prohibit elimination of the requirement that a CDS-built liner vessel be used only for foreign trade.

Sea-Land is quite concerned with the provision of H.R. 2550 that would effectively repeal the protections afforded by Section 805(a) of the Merchant Marine Act, 1936 in the event of CDS payback for non-liner vessels. Section 805(a) makes it unlawful to award or pay operating differential subsidy to any contractor if that contractor, or any affiliate or associate, directly or indirectly owns, operates, or charters any vessel engaged in the domestic intercoastal or coastwise service, without the written permission of the Secretary of Transportation. Section 805(a) mandates a hearing if any person having an interest in an application for permission under Section 805(a) requests such a hearing. This provision has proven to be vitally important in guarding against unfair use of ODS to support the operation of a vessel in domestic service. There has been no sound basis advanced for eliminating the requirements of Section 805(a) in conjunction with liner operations and it is important that this provision of the statute not be altered in that regard. The spectre of subsidized operators of non-liner vessels being permitted to commence domestic liner services without meeting the requirement of Section 805(a) would have a severe chilling effect on new investment in U.S.-built ships for the domestic trades.

The Congress and the Administration should continue to encourage subsidized U.S. carriers to reduce their dependence on ODS. Carriers that terminate their dependence on ODS would no longer need to meet the requirement of Section 805(a). The Government should also encourage construction of modern, fuel-efficient ships in U.S. shipyards for the domestic liner trades, rather than aggravating the overcapacity in the nonsubsidized domestic liner trades by changing the law to allow relatively older, steam-turbine liner vessels unable to compete in foreign commerce to enter the domestic trades.

Thank you for the opportunity to submit our views on CDS payback and H.R. 2485 and H.R. 2550.

Sincerely,

JOSEPH F. ABELY, Jr.,
Chairman and Chief Executive Officer.

HELIOS CAPITAL CORP.,
Radnor, PA, May 22, 1985.

Hon. MARIO BIAGGI,
U.S. House of Representatives, Washington DC.

DEAR CONGRESSMAN BIAGGI: Thank you for your letter, and the invitation to testify at your hearings on CDS payback tomorrow. As always, we appreciate the support we have had from you and from your committee. At present, however, we are still studying the Department of Transportation's new rule, and the various compromise positions which have been suggested, and do not feel ready to testify at present.

Sun still believes that CDS payback is basically arbitrary and inequitable, and that it will damage the maritime industry and hence the national security. We believe that the fiscal benefits cited in the rulemaking have been vastly overstated. Time will doubtless reveal who is right.

We hope that your hearings, and the efforts of your committee, will lead to the adoption of a compromise. We have not yet seen all of the proposals, but we feel very strongly that any compromise must have a stringent time limit as its core. The prime benefit of the one-year window in the new DOT rule is that it offers the operator of Jones Act vessels an end to the continued uncertainty that has prevented forward planning. An open-ended payback would leave a continued overhang of vessels that could come into the market, and would thus preclude any possibility of capital investment. We are concerned, however that fast administrative footwork could permit the extension of this one-year window. We believe that legislation strictly limiting the window for payback and forbidding all payback or waivers thereafter, must be an essential ingredient of any compromise.

As the situation clears, and we complete our study, we will be sure to keep you fully informed as to our position. We will follow your hearings with keen interest.

Thank you again for your supportive stance.

Sincerely,

R. ANDERSON PEW.

DELOITTE HASKINS—SELLS,
New York, NY, April 30, 1985.

INDEPENDENT TANKER OWNERS COMMITTEE,
c/o American Maritime Association, New York, NY.

To Members of the Committee: We are pleased to submit the report on our independent analysis of the impact on Federal Government revenues that could result from the Department of Transportation's proposed rule change regarding the repayment of construction differential subsidies (CDS). The purpose of the CDS is to make U.S. built vessels competitive with foreign built vessels on a construction cost basis.

SCOPE OF STUDY

As we agreed, our analysis was limited to estimating the impact of the proposed CDS rule change on Federal Government revenues. We did not analyze the impact the rule change may have on other parties such as oil producers, independent shipowners, financial institutions or the stockholders of these corporations.

TIME LIMITATIONS

Because of the tight legislative time schedule, we were asked to complete this study in a very short time period (approximately 2 weeks). While we believe the major revenue impact items have been addressed, we can offer no assurances that all significant assumptions upon which the outcome might depend have been identified.

QUALIFICATION REGARDING ESTIMATED REVENUES

In order to quantify the revenue impact of the proposed CDS rule change, we made a number of assumptions which were based upon available independent information and discussions with various knowledgeable individuals such as officials from the Maritime Administration, Department of Defense, leading independent ship owners, and the Shipbuilders Council of America. The revenue impact estimates in this report are based upon these assumptions about conditions and courses of action that we believe are reasonably possible, although not necessarily probable. Some assumptions inevitably will not materialize and unanticipated events and circumstances may occur subequent to April 30, 1985, the date the study was completed. Therefore, the actual results achieved will vary from our estimates and the variation may be material.

This report is based upon information available as of April 30, 1985. We have no responsibility to update this report for events and circumstances occurring after the date of this report.

Yours truly,

DELOITTE HASKINS—SELLS

SUMMARY OF FINDINGS

Based upon our analysis, the Department of Transportation's ("DOT") proposed rule change that would permit shipowners to repay construction differential subsidies ("CDS") would have a negative impact on the Federal Government's revenues ranging from as little as $48.4 million to as much as $476.8 million for the period Fiscal 1986 through Fiscal 1990 (See Schedule 1).

On a net present value basis, discounting the revenue flow at the estimated cost of funds rate to the Federal Government, the negative impact would range from $1.4 million to $411.6 million for the period Fiscal 1986 through Fiscal 1990 (See Exhibit XIV).

Our estimates are based upon a number of key assumptions presented immediately following this summary of findings. It was difficult to determine the probability that certain events may or may not happen as a result of the proposed rule changes. For this reason we calculated a range of possible financial consequences for specific events. When these individual ranges are taken together, they result in the wide range of overall potential financial consequences the wide range of overall potential financial consequences shown above. Accordingly, it is important for the reader of this document to fully understand these key assumptions since the estimated results could vary dramatically depending upon the assumptions used.

RETURN OF CDS PAYMENTS

Our analysis (summarized on Schedules 1, 2 and 3 of this document) indicates that the Federal Government should realize a positive cash flow of approximately $269.6 million directly related to the repayment of CDS from subsidized vessel owners. This amount includes the estimated repayment of the CDS and the elimination of the Operating Differential Subsidy ("ODS") for the thirteen vessels identified by DOT as most likely to repay their CDS amounts. The calculated amount also includes the estimated reduction in tax revenue related to the various tax benefits which would accrue to the subsidized vessel owners as a result of the CDS repayments.

UNEMPLOYMENT IN SHIPBUILDING AND MARITIME INDUSTRIES

The positive cash flow that the Federal Government would realize from the CDS repayments would be more than offset by the potential revenue losses which may occur as a result of the rule change. There are strong indications that the proposed rule change could have a negative impact on employment in both the domestic shipbuilding and maritime industries. The projected surplus of vessels operating in the domestic market will eliminate any incentive to build new unsubsidized domestic vessels. In recent years, expenditures on domestic shipbuilding have averaged approximately $400.0 million per annum (See Exhibit XII). It is estimated that nearly 6,850 shipbuilding and related industry jobs could be lost if the proposed rule change is adopted. In addition, the entry of the CDS vessels into the domestic market will result in the displacement of as many as thirty currently active independent tankers. If this occurs, approximately 1,200 seamen (See Exhibit XIII) would lose their jobs. Assuming that the unemployed could not find other jobs available in the economy, it is estimated that the resulting reduced employment would adversely effect federal income tax revenues by $296.1 million for the period Fiscal 1986 through Fiscal 1990. Therefore, the positive revenue impact of the CDS repayments are more than offset by a greater amount of lost Federal income tax.

CORPORATE INCOME TAXES

The greater cost efficiency of the CDS vessels and the surplus of vessels in the domestic market could have additional negative impacts on the Federal Government's revenue flow. The increased competition among the more efficient vessels would result in lower charter rates thus depressing the profits of the independent shipowners. This reduction in corporate earning will cause a related reduction in federal income taxes (see Exhibit X).

FEDERAL GUARANTEES

There is also a reasonable probability that if charter rates are reduced, shipowners would not generate sufficient funds to cover debt service on the vessels. The Federal Government has guaranteed a significant portion of the debt through the Title XI program. As of September 30, 1985 the total Title XI loan balance on unsubsidized vessels is estimated at $837.0 million. In addition, the Federal Government has guaranteed approximately $156.2 million related to Seatrain Lines, Inc. which is currently operating as a debtor in possession under Chapter XI of the Federal Bankruptcy Law. Defaults on even a small portion of these government backed loans could have a significant impact on the Federal Government's net revenue related to the proposed rule change.

PRIVATE DEBT

Many of the vessels owned by independent shipowners have been financed by financial institutions without government guarantees. Based upon a survey of key independent shipowners, it is estimated that in excess of $400.0 million in existing loans are subject to risk if the rule change is adopted. Defaults on this debt would result in write off expenses to the lenders and correspondingly reduce their income tax liability.

READY RESERVE FLEET

The Merchant Marine has historically been considered an essential component of national defense. In response to the comment that enactment of the proposed rule change would cause scrapping of ships eligible for the Ready Reserve Fleet, proponents of the rule change have suggested that the Ready Reserve purchase these ships and store them until they are needed. Industry estimates are that approximately 20 vessels would be purchased by the Navy. However, we have made a more conservative assumption and have estimated that it is likely the Navy will purchase no more than eight (8) vessels by 1988. The cost to the Federal Government for purchasing and refurbishing these eight vessels is estimated to be five million dollars per vessel.

Our analysis clearly indicates that the proposed rule change will result in a negative impact of federal government revenue. The size of this negative impact will depend upon numerous factors, many of which are impossible to predict with any degree of certainly.

KEY ASSUMPTIONS

Our analysis is based upon a number of key assumptions which are delineated below. The first seven assumptions directly relate to the potential CDS repayments from subsidized vessels owners. These assumptions provide a basis for estimating the net revenue the Federal Government can expect to realize from the CDS repayments. The remaining assumptions address a number of indirect events which may occur as a result of the CDS repayments.

(1) *Thirteen eligible vessels will repay their CDS.*

BEST COPY AVAILABLE

There are twenty-seven vessels which have received CDS payments and are eligible to return the subsidies under the proposed rule change. A complete list of these vessels is presented in Exhibit I. This same exhibit also indicates the thirteen vessels that the Department of Transportation ("DOT") identified as the most probable to repay their CDS. It appears that the DOT has identified the thirteen specific vessels based upon a number of factors including: ownership, vessel capacity (DWT) and contractual commitments (charters). Based upon our review of various documents and conversations with knowledgeable industry individuals (both pro and con the rule change), there appears to be general agreement that these thirteen vessels are the most likely candidates to repay their CDS.

(2) *CDS repayments would occur in Fiscal 1986.*

For purposes of this analysis, it was assumed that the CDS repayments would take place in Fiscal 1986. Under the proposed rule change, each vessel owner would have the right to exercise the repayment option at a time convenient to them. Once the option is exercised, the full CDS payment is due. Therefore, payments actually could occur in more than one fiscal year. Considering the present value effects of such repayments, our assumption that all CDS repayments will occur in Fiscal 1986 maximizes the value of the CDS repayment to the Federal Government.

(3) *The effective federal tax rate for the owners of the thirteen vessels is estimated at 30%.*

Many of the CDS vessels are owned by subsidiaries of larger companies. Other vessels are owned by private companies for which tax information is unavailable. This makes it difficult to evaluate the potential tax effects upon the individual entities which own eligible vessels. However, we have examined recent annual reports and the 1983 DOT Maritime Administration (MARAD) report which presents combined financial statements for 25 subsidized companies. These reports indicate that the average federal tax rate for these companies is approximately 30%.

(4) *The vessel owners will benefit from the tax effect of financing the CDS repayments.*

The estimated CDS repayments will total approximately $377.6 million (See Exhibit I). Under the proposed rule change, the entire CDS amount must be paid to the Federal Government at the time the election is made. The vessel owners will finance the CDS repayments by either borrowing funds or liquidating investments. Regardless of which method is chosen, a reduction in the taxable income of the vessel owners should occur. For purposes of this analysis, we have assumed that funds for repayment would be financed by a five year self-liquidating loan at 10.5% (prime rate at April 19, 1985).

(5) *The equivalent of three of the thirteen vessels would have had Section 506 Waivers during each year of the Fiscal 1986–1990 period.*

Under existing regulations, CDS vessels can apply for a Section 506 Waiver which allows the vessels to operate in the domestic market for up to 6 months during a calendar year. CDS vessels are normally prohibited from operating in the domestic trade. Vessels granted the waiver must repay a pro rate portion of the CDS payment (based upon a 20 year life) for this privilege. Based upon past history (see Exhibit IV), we estimate that, on average, three of the thirteen vessels would be operating under the 506 Waiver at any one time. Therefore, the effect of the proposed rule change would be limited to the difference between the total CDS repayments and the amount that would be collected without the rule change.

(6) *The CDS repayments will entitle the vessel owners to federal tax deductions equal to the amount of the repayments ($377.6 million).*

The actual amount and timing of the tax deductions will depend upon the individual tax situation of each vessel owner. For purposes of this analysis, we assumed that the tax deductions will be used evenly over the five year period from Fiscal 1986 to Fiscal 1990.

(7) *The Federal Government will save $95.2 million for the period Fiscal 1986 through Fiscal 1990 due to the elimination of the Operating Differential Subsidies ("ODS") for the thirteen vessels.*

Operating Differential Subsidies are amounts paid to the owners of subsidized vessels to offset the higher cost of operating in the foreign trade under the American flag, compared to the cost of operating under a foreign flag. ODS amounts are not granted to vessels operating in the domestic trade.

Exhibit II indicates the actual level of ODS for the thirteen vessels for the periods Fiscal 1979 through Fiscal 1983. We have used an average of the last two years ODS payments and an inflation factor of 5% as a basis for projecting the payments for the Fiscal 1986 through 1990 period.

(8) *The entry of the thirteen CDS vessels into the domestic market will create a surplus of domestic vessels thereby reducing the demand for new vessels. This will result in increased unemployment in the shipbuilding industry.*

In recent years, expenditures for domestic shipbuilding activities have averaged approximately $400 million per annum (See Exhibit XII). Experts from the shipbuilding industry including Mr. Lee Rice, President of the Shipbuilders Council of America and Mr. Frank Drozak, President of the Seafarers International Union of North America, AFL–CIO, have testified before Congress that the proposed rule change would eliminate new production of unsubsidized vessels for the next ten years.

(9) *The entry of the thirteen CDS vessels into the Alaskan North Slope (ANS) market will have a bumping effect on the domestic market resulting in the elimination of approximately 30 domestic vessels. This will result in increased unemployment in the maritime industry due to the layoff of the crews of these vessels.*

Based upon the average crew size, and the anticipated number of ships to be bumped, we estimate that approximately 1,215 seamen (see Exhibit XIII) are likely to lose their jobs.

(10) *The estimated effective Federal tax rate is 16% for shipbuilders and related industry employees and 25% for maritime seamen.*

These estimates are based upon the Federal Tax Tables for the average income of these workers.

(11) *Due to their size, the CDS vessels expected to enter the domestic market are generally more efficient on an operating cost basis than many of the smaller unsubsidized tankers currently in the market. This efficiency, along with a surplus of vessels in the market, would probably result in lower charter rates. Under these conditions, it is likely that there would be defaults on government backed debt (Title XI and other government guarantees) and debt to private financial institutions.*

At September 30, 1985, the Federal Government will have contingent liabilities of approximately $837.0 million of outstanding debt attributable to Title XI debt on current active, unsubsidized tankers. For analysis purposes, we have assumed the potential defaults could range between 0% and 10% of such debt; i.e.,—$0 to $83.7 million.

Government Guaranteed Debt—including Economic Development Authority Loans, and MARAD Notes Payable in an amount estimated to be at risk of approximately $156.2 million.

Debt Owed to Various Financial Institutions—total debt identified by management representatives of tanker owners which may be at risk is estimated to be approximately $420 million. After discounting such debt by the effective tax rate for large financial institutions (approximately 25%), it appears that the overall potential tax loss attributable to debt at risk under the proposed CDS repayment proposal could be as high as $105 million.

(12) *The entry of the thirteen CDS vessels into the domestic market will cause charter rates to fall. This will result in reduced profits and correspondingly lower Federal Corporate income tax liability.*

In testimony before Congress, several officers of companies owning vessels have indicated that the proposed rule change would result in lower corporate profit and federal income tax liability.

Exhibit XI indicates the results of a recent telephone survey of senior financial personnel of companies believed likely to have their corporate income tax payments reduced or eliminated by the rule change. The listed amounts represent either the projected reduction of Federal income tax liability or reduction of a parent's Federal income tax liability in the case of a subsidiary currently operating at a loss (where the parent has taxable income).

(13) *The Ready Reserve Fleet is likely to purchase eight (8) tankers of less than 90,000 DWT by 1988. The cost to the Federal government of obtaining and refurbishing the tankers is estimated to be $5 million per vessel.*

It has been suggested that displaced vessels would be absorbed by the Ready Reserve Fleet: Based upon available information, the Navy would like to add sixteen vessels to the Ready Reserve Fleet between Fiscal 1986 and 1988. It already has commitments for eight vessels. The need for eight remaining vessels could be filled with eight vessels meeting the Navy's standards, displaced from domestic trade. However, the Navy is not obligated to purchase any vessels and will do so only if funds are appropriated.

(14) *A 5% annual inflation factor was used for estimating Operating Differential Subsidies (ODS) and shipbuilding and seaman wages.*

SCHEDULE 1.—SUMMARY OF IMPACT ON FEDERAL REVENUE

[In millions of dollars]

Federal Goverment, net revenue	Fiscal years 1986–90	
	Low	High
Increase directly related to CDS repayments (schedule 2)	269.6	269.6
Decrease indirectly related to CDS repayments (schedule 3)	(318.0)	(746.4)
Net revenue increase (decrease)	(48.4)	(476.8)

SCHEDULE 2.—FEDERAL GOVERNMENT NET REVENUE INCREASE DIRECTLY RELATED TO CDS REPAYMENTS

[In millions of dollars]

	Fiscal year					Total 1986–90
	1986	1987	1988	1989	1990	
Return of CDS funds (1):						
Principal	157.0					157.0
Interest	220.6					220.6
Elimination of operating differential subsidy ("ODS") (2)	17.2	18.1	19.0	20.0	20.9	95.2
Foregone CDS section 506 waiver payments (3)	(4.6)	(4.6)	(4.6)	(4.6)	(4.6)	(23.0)
Federal tax deducations for owners of CDS vessels related to CDS payments:						
Amortization of CDS payback (4)	(22.7)	(22.7)	(22.7)	(22.7)	(22.7)	(113.5)
Tax effect of ODS elimination (5)	(5.2)	(5.4)	(5.7)	(6.0)	(6.3)	(28.6)
Tax deductions for owners of CDS vessels related to financing CDS repayments:						
Interest on borrowed funds or income lost due to use of Funds (6)	(11.9)	(10.0)	(7.8)	(5.5)	(2.9)	(38.1)
Net revenue to Federal Government from owners repaying CDS	350.4	(24.6)	(21.8)	(18.8)	(15.6)	(269.6)

(1) Exhibit I.
(2) Exhibit II.
(3) Exhibit III and IV.
(4) Exhibit V.
(5) Exhibit VI.
(6) Exhibit VII.

SCHEDULE 3.—FEDERAL GOVERNMENT NET REVENUE DECREASE INDIRECTLY RELATED TO CDS REPAYMENTS

[In millions of dollars]

	Fiscal year										Total	
	1986		1987		1988		1989		1990		1986–90	
	Low	High	Low	High	Low	High	Low	High	Low	High	Low	High
Income tax reduction arising from increased unemployment [1]:												
Shipbuilding and related industries	38.4	38.4	40.3	40.3	42.3	42.3	44.4	44.4	46.6	46.6	212.0	212.0
Maritime industry	15.2	15.2	16.0	16.0	16.8	16.8	17.6	17.6	18.5	18.5	84.1	84.1
Subtotal	53.6	53.6	56.3	56.3	59.1	59.1	62.0	62.0	65.1	65.1	296.1	296.1
Other items:												
Potential title XI defaults on unsubsidized tankers [2]	0.0	27.9	0.0	27.9	0.0	27.9					0.0	83.7
Other defaults (Government guarantees) [3]	0.0	156.2									0.0	156.2

SCHEDULE 3.—FEDERAL GOVERNMENT NET REVENUE DECREASE INDIRECTLY RELATED TO CDS REPAYMENTS—Continued

[In millions of dollars]

	Fiscal year										Total	
	1986		1987		1988		1989		1990		1986–90	
	Low	High	Low	High	Low	High	Low	High	Low	High	Low	High
Other defaults (Financial institutions) [3]	0.0	35.0	0.0	35.0	0.0	35.0					0.0	105.0
Cost of Ready Reserve fleet expansion [4]	0.0	10.0	0.0	15.0	0.0	15.0					0.0	40.0
Reduced corporate income taxes [5]	3.0	9.0	5.4	16.1	6.1	18.3	4.7	14.0	2.7	8.0	21.9	65.4
Subtotal	3.0	238.1	5.4	94.0	6.1	96.2	4.7	14.0	2.7	8.0	21.9	450.3
Total	56.6	291.7	61.7	150.3	65.2	155.3	66.7	76.0	67.8	73.1	318.0	746.4

[1] Exhibit VIII.
[2] Exhibit XI.
[3] Assumption II.
[4] Exhibit XI.
[5] Exhibit X.

EXHIBIT I.—ELIGIBLE CDS VESSELS

[Dollar amounts in millions]

Vessel name; year built; current owner	DWT	CDS repayment anticipated	Vessel returning subsidy		
			As of Sept. 30, 1985		DWT
			Unamortized CDS	Interest	
ARCO Independence; 1977; Atlantic Richfield	262,400	Yes	$21.3	$23.0	262,400
ARCO Spirit; 1977; Atlantic Richfield	262,400	Yes	21.2	22.2	262,400
American Heritage; 1976; Atlas Marine (Berger Group)	91,800	Yes	7.8	7.2	91,800
Atlantic; 1980; Hartford National Bank	390,000	No			
Beaver State; 1976; American Shipping (Berger Group)	91,800	Yes	7.8	8.6	91,800
Brooklyn; 1973; American Petrofina	226,200	Yes	8.1	12.9	226,200
Chelsea; 1975; Margate Shipping Co.	39,000	No			
Cherry Valley; 1974; Margate Shipping Co.	39,000	No			
Chestnut Hill; 1976; Chestnut Shipping Co.	91,300	Yes	7.6	8.5	91,300
Coronado; 1973; Margate Shipping Co.	39,000	No			
Courier; 1981; Ogden Courier Transport (OMI)	35,000	No			
Golden Endeavor; 1974; Aeron Marine (Berger Group)	91,800	Yes	7.5	10.9	91,800
Golden Monarch; 1975; Aquarias Marine (Berger Group)	91,400	Yes	8.2	10.6	91,400
Kittaning; 1976; Chestnut Shipping Co.	91,300	Yes	8.3	8.1	91,300
Maryland; 1976; Seatrain Lines	264,100	Yes	17.8	25.0	264,100
Massachusetts; 1975; Seatrain Lines	264,100	Yes	16.2	28.9	264,100
MormacSky; 1975; Moore McCormack	39,700	No			
MormacStar; 1975; Moore McCormack	39,700	No			
MormacSun; 1975; Moore McCormack	39,700	No			
New York; 1976; Seatrain Lines	264,100	Yes	13.0	29.8	264,100
Pacific; 1981; Hartford National Bank	390,000	No			
Patriot; 1981; Ogden Patriot (OMI)	35,000	No			
Ranger; 1981; Ogden Ranger (OMI)	35,000	No			
Rover; 1981; Ogden Rover (OMI	35,000	No			
Ul tramar; 1973; Aries Marine (Berger Group)	82,100	No			
Ul trasea; 1974; Aries Marine (Berger Group)	82,100	No			
Williamsburgh; 1974; American Petrofina	255,100	Yes	12.2	24.9	255,100
Total;			$157.0	$220.6	2,347,800
Total Repayment				$377 6	

EXHIBIT II.—OPERATING DIFFERENTIAL SUBSIDIES (ODS) FOR VESSELS EXPECTED TO REPAY CONSTRUCTION DIFFERENTIAL SUBSIDIES (CDS)

[In millions of dollars]

Actual		Estimated	
Fiscal year	ODS payments	Fiscal year	ODS payments
1979	9.1	1986	[1] 17.2
1980	12.6	1987	[2] 18.1
1961	13.5	1988	[2] 19.0
1982	16.5	1989	[2] 20.0
1983	17.8	1990	[2] 20.9
Total	69.5		95.2
Average per year	13.9		19.0

[1] Based upon average ODS for last 2 years of actuals (fiscal 1982 and 1983).

[2] Assumes a 5 percent inflation factor.

EXHIBIT III.—*Estimated foregone section 506 waiver payments*

Vessel (VLCC's):	*Original CDS grants (millions)*
Arco Independence	$35.6
Arco Spirit	$35.4
Brooklyn	$20.3
Maryland	$32.4
Massachusetts	$32.4
New York	$32.4
Williamsburgh	$27.2
Total CDS grants	**$215.7**
Total CDS per year ($215.7 divided by 20 years)	**$10.8**
Average section 506 waiver payment per ship (10.8 divided by seven ships)	**1.54**
Estimated number of equivalent vessels [1] that would receive section 506 waivers each year (Fiscal 1986–90)	**3**
Estimated annual CDS repayments for the periods Fiscal 1986 through 1990	**4.6**

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[1] Equivalent vessels—section 506 Waivers are granted for 6 month periods. The above calculations assume that six vessels will receive waivers each year thus equating to three full time vessels. See exhibit IV for recent history of section 506 waivers granted.

EXHIBIT IV.—PAST SECTION 506 WAIVER IN ALASKAN NORTH SLOPE TRADE

Vessel	DWT (thousands)	Type	Dates of operation under 506 waiver	
			From	To
American Independence (now Arco Independence)	265.0	VLCC	March 17, 1978	September 18, 1978.
American Independence (now Arco Independence)			March 3, 1980	September 5, 1980.
American Independence (now Arco Independence)			September 23, 1981	March 18, 1982.
ARCO Independence (ex-American Independence)			October 1, 1982	
American Spirit (now Arco Spirit)	265.0	VLCC	January 2, 1978	March 1, 1978.
American Spirit (now Arco Spirit)			February 18, 1979	March 9, 1979.
American Spirit (now Arco Spirit)			March 23, 1979	April 13, 1979.
American Spirit (now Arco Spirit)			December 19, 1979	June 13, 1980.
American Spirit (now Arco Spirit)			January 24, 1981	July 22, 1981.
Arco Spirit (ex-American Spirit)			March 21, 1982	September 19, 1982.
Brooklyn	228.0	VLCC	December 25, 1979	June 12, 1980.
Brooklyn [1]			February 14, 1981	September 6, 1981.

EXHIBIT IV.—PAST SECTION 506 WAIVER IN ALASKAN NORTH SLOPE TRADE—Continued

Vessel	DWT (thousands)	Type	Dates of operation under 506 waiver	
			From	To
Brooklyn			May 24, 1982	November 28, 1982.
Maryland	265.0	VLCC	April 3, 1978	October 9, 1978.
Maryland			August 25, 1979	March 31, 1980.
Maryland			November 4, 1980	May 10, 1981.
Maryland			November 19, 1981	April 24, 1982.
Maryland			October 28, 1982	
Massachusetts	265.0	VLCC	June 27, 1978	January 10, 1979.
Massachusetts			December 19, 1978	June 21, 1980.
Massachusetts			January 1, 1981	March 7, 1981.
New York	265.0	VLCC	August 19, 1977	November 12, 1977.
New York [2]			July 16, 1980	February 15, 1981.
New York			May 22, 1982	November 9, 1982.
Williamsburgh [1]	225.0	VLCC	May 29, 1980	December 1, 1980.
Williamsburgh			January 15, 1982	May 8, 1982.
Williamsburgh			November 23, 1982	
Beaver State [3]	89.7	Panamax	January 25, 1979	February 18, 1979.
Beaver State			February 19, 1979	March 4, 1979.
Beaver State			February 25, 1982	April 27, 1982.
Chestnut Hill [3]	89.7	Panamax	February 18, 1978	March 5, 1978.
Kittaning [3]	89.7	Panamax	March 30, 1982	April 18, 1982.

[1] Includes one intermediate foreign trade voyage.

[2] Includes oil storage in Delaware Bay.

[3] Panamax size tankers are granted section 506 waivers only during times of extreme shortages of vessels. Therefore, we did not include them in our base data for projecting future waivers.

Source: "Oil Tankers Built with CDS", Marad's Office of Associate Administrator for Maritime Aids, July 28, 1982 and updated version.

EXHIBIT V.—ESTIMATED TAX EFFECT RELATED TO AMORTIZATION OF CDS REPAYMENT OVER A 5-YEAR ESTIMATED ECONOMIC LIFE

[Dollar amounts in millions]

Year	CDS Repayments		Amortization deduction	Estimated	
	Total amount [1]	Amortization rate [2] (percent)		Effective tax rate [3] (percent)	Tax effect
1986	$377.6	20	$75.5	30	$22.7
1987	377.6	20	75.5	30	22.7
1988	377.6	20	75.5	30	22.7
1989	377.6	20	75.5	30	22.7
1990	377.6	20	75.5	30	22.7
Total		100	377.6		113.5

[1] Exhibit I.

[2] Assumption No. 6.

[3] Assumption No. 3.

EXHIBIT VI.—ESTIMATED TAX EFFECT RELATED TO THE ELIMINATION OF THE OPERATING DIFFERENTIAL SUBSIDIES (ODS)

[Dollar amounts in millions]

Year	ODS payments eliminated [1]	Effective tax rate [2] percent	Tax effect of ODS elimination
1986	$17.2	30	$5.2
1987	18.1	30	5.4

EXHIBIT VI.—ESTIMATED TAX EFFECT RELATED TO THE ELIMINATION OF THE OPERATING DIFFERENTIAL SUBSIDIES (ODS)—Continued

[Dollar amounts in millions]

Year	ODS payments eliminated [1]	Effective tax rate [2] percent	Tax effect of ODS elimination
1988	19.0	30	5.7
1989	20.0	30	6.0
1990	20.9	30	6.3
Total	95.2		28.6

[1] Exhibit II.
[2] Assumption No. 3.

EXHIBIT VII.—ESTIMATED TAX EFFECT OF INTEREST RELATED TO FINANCING CDS REPAYMENTS

[Dollar amounts in millions]

Fiscal year	Repayment of Loan [1]		Estimated	
	Principal	Interest	Effective tax rate [2] (percent)	Tax effect
1986	$61.3	$39.7	30	$11.9
1987	67.7	33.3	30	10.0
1988	74.8	26.1	30	7.8
1989	82.6	18.3	30	5.5
1990	91.2	9.6	30	2.9
Total	$377.6	$127.0		$38.1

[1] Exhibit No. 1 plus assumption No. 4.
[2] Assumption No. 3.

EXHIBIT VIII.—INCOME TAX EFFECT OF INCREASED UNEMPLOYMENT

	Shipbuilders and related industry	Seamen
(A) Estimate for Fiscal 1986		
Estimated increase in unemployment	6,857	1,215
Estimated average annual wages	$35,000	$50,000
Total wages lost	$240,000,000	$6,750,000
Assumed tax rate (percent)	16%	25%
Total estimated income tax lost	$38,400,000	$15,187,500
(B) Estimate for Subsequent Fiscal Years [1]		
Fiscal year:		
1986 (from above)	$38.4	$15.2
1987	40.3	16.0
1988	42.3	16.8
1989	44.4	17.6
1990	46.6	18.5
Total	212.0	84.1

[1] Assumption No. 14 (5 percent inflation factor).

EXHIBIT IX.—POTENTIAL TITLE XI DEFAULTS CURRENT ACTIVE UNSUBSIDIZED TANKERS

[In millions of dollars]

	ANS	Other trades	Total
Original title XI balance	874.5	334.0	1,208.5
Balance at Sept. 30, 1984	641.8	255.6	897.4
Less: 1/20 of original balance assuming a 20-year life	43.7	16.7	60.4
Estimated balance at Sept. 30, 1985	598.1	238.9	837.0

Potential title XI amounts at risk

	Millions
At 100 percent	$837.0
At 90 percent	753.3
At 80 percent	669.6
At 70 percent	585.9
At 60 percent	502.2
At 50 percent	418.5
At 40 percent	334.8
At 30 percent	251.1
At 20 percent	167.4
At 10 percent	83.7
At 5 percent	41.9
Title XI defaults sensitivity range:	
Minimum annual defaults (at 0 percent of Sept. 30, 1985 balance)	0.0
Maximum assumed defaults (at 10 percent of Sept. 30, 1985 balance)	83.7
Estimated defaults per year (assuming defaults occur in first 3 years (1986–88))	27.9

EXHIBIT X.—ESTIMATED REDUCTION IN CORPORATE INCOME TAX PAYMENTS

[In millions of dollars]

	Fiscal years					Total
	1986	1987	1988	1989	1990	
Company 1		3.0	5.0	5.0		13.0
Company 2	2.0	3.5	3.5			9.0
Company 3	1.0	1.0	1.0	1.0	1.0	5.0
Company 4	1.5	1.6	1.8	2.0	2.0	8.9
Company 5						
Company 6	1.5	1.5	1.5	1.5	1.5	7.5
Company 7	2.0	3.5	3.5	3.5	3.5	16.0
Company 8	1.0	2.0	2.0	1.0		6.0
Net reduction in corporate income tax payments (high range)	9.0	16.1	18.3	14.0	8.0	65.4
Estimated minimum reduction (low range) equal to 33⅓ percent of high range total	3.0	5.4	6.1	4.7	2.7	21.9

Note.—We obtained this data by means of a telephone survey of eight companies which asked not to be identified. Estimates were provided by senior fianncial officers of annual amounts by which they reasonably expect that their Federal income taxes payable may be reduced.

EXHIBIT XI.—ESTIMATED COST OF READY RESERVE FLEET EXPANSION

[Dollar amounts in millions]

	Fiscal years					Total
	1986	1987	1988	1989	1990	1986–90
Estimated number of ships acquired by Ready Reserve Fleet	2	3	3	0	0	8
Cost per ship	$5	$5	$5	0	0	$5
Total cost of Ready Reserve Fleet expansion	$10	$15	$15	0	0	$40

EXHIBIT XII.—*ACTUAL EXPENDITURES ON UNSUBSIDIZED VESSELS BUILT IN THE UNITED STATES*

[In millions of dollars]

	Actual[1]
1975	190
1976	145
1977	375
1978	725
1979	355
1980	215
1981	675
1982	340
1983	450
1984	315
Total	3,785
Retrofits per Port and Tanker Safety Act	200
Total	[2] 3,985

[1] Based upon a list of vessels built each year and their approximate cost. Amounts were also confirmed during discussions with Mr. Lee Rice, president of the Shipbuilders Council of America.

[2] Approximately $400 million per year.

EXHIBIT XIII.—*ESTIMATED JOBS LOST BY SEAMEN*

Number of ships estimated to be displaced	30
Number of billets (crew stations) per ship	27
Subtotal	810
Crewmembers required per billet	×1.5
Total	1,215

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EXHIBIT XIV.—PRESENT VALUE OF ESTIMATED NET DISCOUNTED REVENUE LOSS

[Dollar amounts in millions]

	Fiscal year										Total [1]	
	1986		1987		1988		1989		1990		1986–1990	
	Low	High	Low	High	Low	High	Low	High	Low	High	Low	High
Net revenue flow (loss):												
Directly related to CDS repayments (schedule 2)	$350.4	$350.4	($24.6)	($24.6)	($21.8)	($21.8)	($18.8)	($18.8)	($15.6)	($15.6)	$269.6	$269.6
Indirectly related to CDS repayments (schedule 3)	($56.6)	($291.7)	($61.7)	($150.3)	($65.2)	($155.3)	($66.7)	($76.0)	($67.8)	($73.1)	($318.0)	($746.4)
Total	$293.8	$58.7	($86.3)	($174.9)	($87.0)	($177.1)	($85.5)	($94.8)	($83.4)	($88.7)	($48.4)	($476.8)
Discount rate (factor) [1]		1.000		.941		.886		.834		.786		
Discounted value	$293.8	$58.7	($81.2)	($164.6)	($77.1)	($156.9)	($71.3)	($79.1)	($65.6)	($69.7)	($1.4)	($411.6)

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[1] Based upon the average of the U.S. Office of Management and Budget's (OMB) estimates for 91 day U.S. Treasury Bill notes for the fiscal years 1986–90 as presented in the April update of the proposed fiscal year 1986 Federal budget.